REAL ESTATE

Vol. 4, No. 5

OUTLOOK

May 1991

A Monthly Forecast for the Economy and Real Estate

FORECAST SUMMARY

- While attention remains fixed on the departing recession, the recovery is expected to steal upon the stage quietly and will take some time to be recognized. After months of deteriorating conditions, the economy fell into the recession with a bang. Several factors, namely war preparations, the federal budget deal, soaring gas prices, and a resulting decline in consumer confidence, trumpeted the onset of the recession.

- In the meantime, signs of recovery will be countered by signs of continued decline. For example, the unemployment rate fell 0.2 percentage points in April, but at the same time, payroll employment declined. Sales of both new and existing homes have moved up in the past two months, but auto sales dropped another notch. All of this amounts to a standstill in in economic growth in the second quarter, according to the NAR forecast.

- After February's impressive performance, housing starts retreated in March, dropping 9.3 percent to an annual rate of 901,000 units. Weakness occurred in the construction of both single and multifamily structures. While the March figures are disheartening, they remain above January's low figures, and support the view that January's dismal performance was the nation's low point.

- Meanwhile, both new and existing home sales held steady in March, after increasing in February. A few key factors appear to be contributing to this renewed activity, notably lower mortgage rates and growing consumer confidence in the economy. Buoyed by robust activity in the West, new home sales increased one percent in March to an annual rate of 490,000 units. After increasing 9 percent in February, sales of existing single-family homes increased 0.6 percent in March, to an annual rate of 3.18 million units.

- Median home prices for both new and existing single-family homes increased in March. The median price of an existing single-family home increased to $96,500, 2.7 percent above February's median price of $94,000. In the market for new single-family homes, the median price increased 4.2 percent, to $125,000 in March. Modest appreciation is expected this year, with the median price of an existing single-family home projected to increase by 1.9 percent, and 3.4 percent for a new single-family home.

IN THIS ISSUE

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The Clan of the Cave Economist, or Dem Bones, Dem Bones, Dem Dry Bones

by John A. Tuccillo
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Deep in the Rift Valley of East Africa, the cradle of humanity, a team of eminent paleontologists have made a discovery that is likely to add significantly to our understanding of how mankind evolved. Following the chance discovery of a cave mouth by a local herdsman, the scientists have uncovered an ancient burial site of *homo economicus,* an obscure and little understood branch of early man, that functioned side by side with *homo sapiens*. In fact, the burial site contained three of the multitude of subspecies that characterize the species. All appeared to have been put to death in particularly grisly fashion.

But perhaps of greatest significance was the discovery of tablets containing in crude pictographs the circumstances of the execution of the *economici*. Here, scientists hope, can be found the reasons why our ancestors had such a difficult time dealing with them.

We know from earlier finds that *homo economicus* served a peculiar function in the primitive clan. Essentially, the members of the clan relied on him for a mixture of present description and soothsaying. Unfortunately, these records indicate, *homo economicus* was terrible at the latter, yet continued to receive the respect of the clan. Scientists have found this aspect of early society particularly confusing, especially in light of the fact that other useless clan members were quickly eliminated.

The tablets discovered at the grave tell a tale of a clan council convened to deal with an important problem. It seems that after eight solid years of great hunting, good crops and a general increase in the well-being of the clan, things had changed. Now, fewer of the clan went out to hunt, the results were meager, and agriculture waned. And, to its great humiliation, the clan had to rely on the support of other clans to maintain its prosperity. Now, they had come together to ask their advisors why this had come to pass and what would happen next.

The first to speak was *homo economicus pollyanacus*. This subspecies lived with the chief of the clan, and served the needs of the chief to have a positive slant on his actions. In other burial sites, *pollyanacus* remains were often found with small mastodon statues and short clubs tipped with flat pieces of iron. *Pollyanacus* maintained that the current lull in hunting results was temporary and would end in the next day or two. Because the clan leaders, in their wisdom, took less and less of the daily kill, the last eight years had placed the clan in an ideal position to prosper forever. Soon, more and more of the clan would go out to hunt and gather and the good days would come back. The people heard this and were glad. They spoke of feeling better and resolved to hunt more and make the earth produce its bounty.

Next to speak was *homo economicus pessimisticus*, the largest of the subspecies. This group tended to grow facial hair as a regular practice and specialize in the training of the clan's youth. Rarely part of the main ruling elite of the clan, *pessimisticus* instead hung at the fringes of the clan, associating primarily with the grumblers and those who carried news from clan to clan.

According to the tablets, *pessimisticus* spoke at nearly interminable length about all the things that were wrong with the clan. The prosperity of the past eight years had been an illusion bought at the price of the clan's future. Present consumption had been increased only because the clan was willing to sell its resources and assets to other clans.

Now, the people did not hunt because those other clans owned all the hunting grounds. This was no temporary lull, but a longer term fault in the clan itself. The people heard this and were afraid. They remembered the time many years ago when a clan leader from a Southern family said the same things and they came true.

Finally, *homo economicus monetarycus* arose. These were the most respected of the *economici*. They lived in the holy place and took counsel with none of their brethren. Rather, they passed the wisdom down one to another and through their incantations made the people of the clan act in certain ways. There is a problem, *monetarycus* said, because the people don't have sufficient reason to hunt or till. They fear the future and feel guilty about their actions in the past.

The leaders of the tribe urged *monetarycus* to utter the spell that would get the people to hunt and farm again, but he hesitated, arguing that too powerful a spell could cause a reaction that would require that two hunters, not one, were necessary to provide an antelope. This had nearly killed the clan in the past.

At this point, the tablets have some significant gaps. But, when the narrative resumes, *monetarycus* has been persuaded to utter the sacred words and some of the clan responds, not by hunting more, but by creating new caves. This helps, and eventually the clan becomes more active, although it never quite reaches the glories of the past period.

The tablets also reveal that the quarrels among the *economici* continued in later clan gatherings until the people and the leaders got so confused, frustrated and upset, that the chief ordered the execution of them all.

Further analysis of the tablets found at the gravesite has convinced the paleontologists that this episode represented the last vestige of *homo economicus* in the history of humanity. Paleontology is still far from an exact science.

Outlook for the Economy and Real Estate

After months of deteriorating conditions, the economy fell into the recession with a bang. There was the drama of war preparations, the federal budget deal, the soaring gas prices -- it's no wonder consumer confidence plummeted so fast. While none of these were prime causes of the recession, they did trumpet its onset. Now, as we wait for the next turning point, the headlines are unlikely to herald the return of growth. Instead, the recovery will steal upon the stage quietly, while attention remains fixed on the cacophony of the departing recession. And as the various sectors of the economy respond to improved economic health, the upswing will take some time to be recognized.

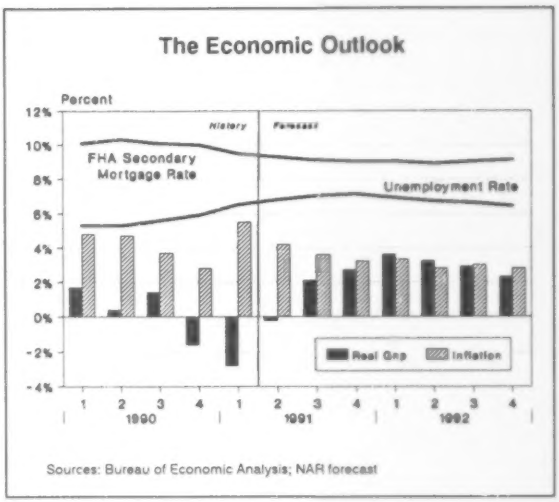
In the meantime, the signs of recovery will be countered by signs of continued decline. For example, the unemployment rate fell 0.2 percentage points in April, but at the same time payroll employment declined. Sales of both new and existing homes have moved up in the past two months, but auto sales dropped another notch. All of this amounts to a standstill in economic growth in the second quarter, according to the NAR forecast. Output is anticipated to drop at a miniscule 0.2 percent annual rate, and the recovery is expected to take hold during the third quarter. A 2.4 percent annual growth rate is projected in the second half of 1991; the economy is then expected to post a solid 2.8 percent growth rate in 1992.

Domestic Spenders Sapped

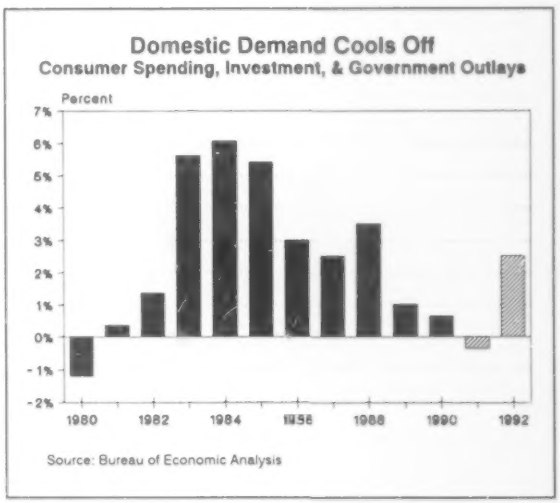
Underscoring the point that the Persian Gulf crisis was not the primary cause of the expansion's end is the official designation of July 1990 as the month the recession began. While the Iraqi invasion in August and the run-up in oil prices (which began in late July) may have turned a brief downturn into a deeper recession, the U.S. expansion was already winded by July. It lasted a marathon 92 months and was second only to the 106-month expansion of the 1960s, which was fueled in part by war expenditures.

Consumers, businesses, and governments appear to be retrenching in the early 1990s. Growth in the demand for goods and services from these three sectors -- known as domestic demand -- wound down in the late 1980s, as the chart at right shows. In 1991, growth in domestic demand is likely to turn negative. Hampered by the S&L bailout, higher oil prices, higher taxes, and preparations for war, the economy in 1990 didn't have enough muscle to reverse such a fundamental trend. What caused domestic demand growth to slide? One leading suspect is the Federal Reserve's inflation-fighting "soft landing" policy that sent short-term interest rates up in the late 1980s; another prime suspect is the increasing debt leverage ratios of the 1980s, which left all three sectors short of breath.

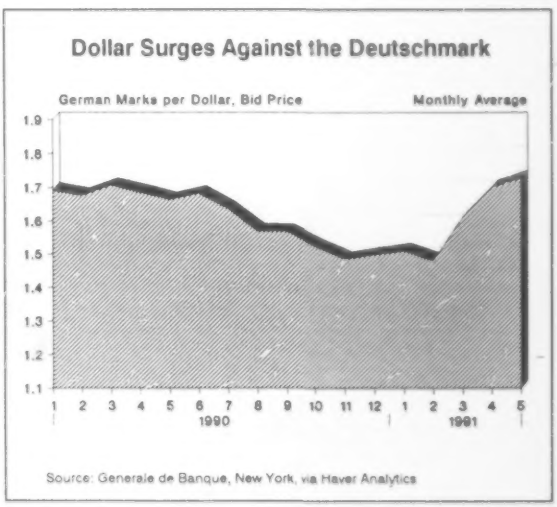
As domestic demand waned in recent years, continued growth in the economy became increasingly reliant on foreign demand. Rising exports played an important role in continuing the expansion at several key points and are expected to contribute significantly in the coming recovery. But the growing prospect of recession in Germany and Japan, joining slumps already underway in the United Kingdom, Austraila and Canada, poses an important risk for the expected recovery. Also threatening foreign demand is the dollar's recent resurgence. The rise of the



Sources: Bureau of Economic Analysis; NAR forecast



Source: Bureau of Economic Analysis



Source: Generale de Banque, New York, via Haver Analytics

dollar -- it's moved up 15 percent against the German Deutschmark since the year began -- effectively lowers the cost to U.S. consumers of imported goods but also raises the price of American goods overseas.

Growth To Remain Below Par For Fifth Consecutive Year

This downturn is nearing the 11-month length of the average recession, but it is still substantially shallower. The drop in output in the eight previous postwar recessions averages 2.6 percent; the current recession is expected to see a drop of 1.2 percent. Of greater concern, however, is the extended period of slow growth, seen in the chart at right. Since early 1988, the U.S. economy has not had even one quarter of growth that exceeded the average growth rate achieved during the 1983-89 period. A subdued recovery will continue this period of restrained growth through 1992. Five years of mediocre performance is a weak foundation for growth in jobs, personal income, and housing, among other areas of the economy.

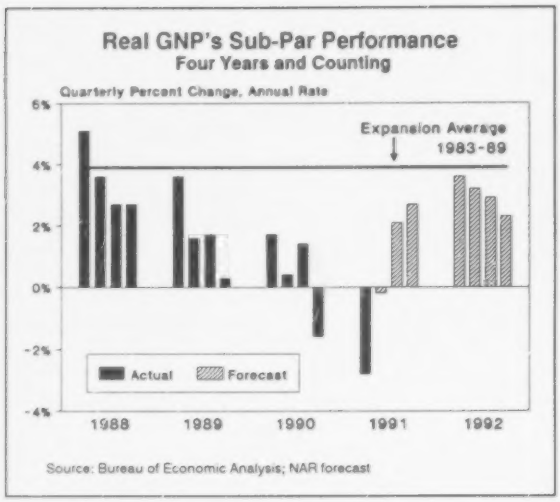
Unemployment Rate Drops to 6.6 Percent

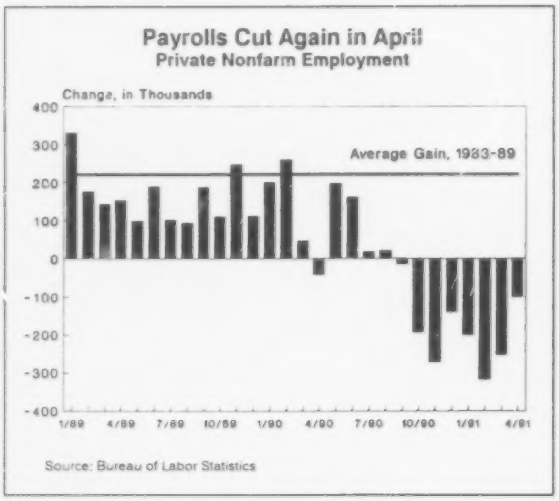
Employment figures released in early May contained a surprising fall in the unemployment rate to 6.6 percent from 6.8 percent. Many analysts had expected to see the rate rise to 7.0 percent, but increases in government hiring and self-employment apparently turned the rate down. Among payroll employees, another 125,000 workers lost their jobs in April, but the decline was only half of the average loss seen in the first three months of 1991.

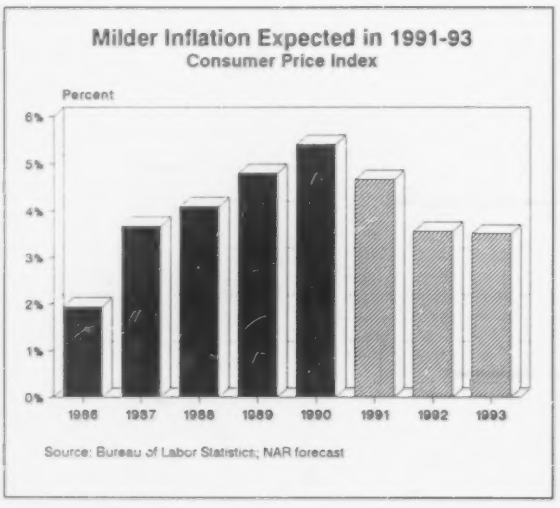
Since it generally continues to fall for a few months after the economy begins to turn up, employment is a lagging indicator of the economy's health. Before hiring more workers, businesses generally increase output by lengthening the workweek and asking current workers to put in more overtime. In April, both the manufacturing workweek and factory overtime rose by 0.1 hour. Since these measures directly tell of activity on the factory shop floor, they're more robust indicators of current economic conditions than changes in consumer confidence and the stock market. Because of their psychological content, these two latter measures have more value in projecting the direction of the economy over the next several months than in assessing current conditions.

Why The Fed Isn't Too Quick to Ease

While the recession is taking its toll on employment, it's also taming inflation, which is expected to fade a bit over the next couple of years. After accelerating in each of the past four years, growth in the Consumer Price Index is expected to ease to 4.7 percent in 1991 from its 5.4 percent clip in 1990. Two years of 3.5 percent gains are anticipated in 1992 and 1993. This is not the price stability that the Federal Reserve is seeking, and it's one reason the Fed is currently hesitant to ease credit any further. In judging the balance between ease and restraint, the monetary authorities are well aware that the effects of changes in monetary policy take time to work their way through the economy. Adding extra credit now, before earlier changes in policy have had a chance to work, may not aid the recovery while risking higher inflation later.







Housing Starts

(Seasonally Adjusted Annual Rates, in Thousands)

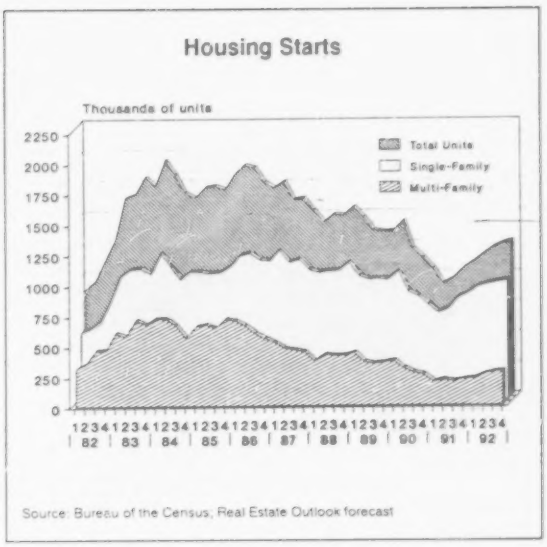
National Data

	Total	SF	2-4	5+
Mar 1990	1,298	988	35	275
Nov 1990	1,130	769	54	307
Dec 1990	971	751	17	203
Jan 1991	847	648	29	170
Feb 1991	993	778	42	173
Mar 1991	***901***	***732***	***28***	***141***
Annual Averages:				
1989	1,381	1,005	56	320
1990	1,203	901	37	265
Percent Changes in March 1991 since:				
Mar 1990	-30.6	-25.9	-20.0	-48.7
Feb 1991	-9.3	-5.9	-33.3	-18.5

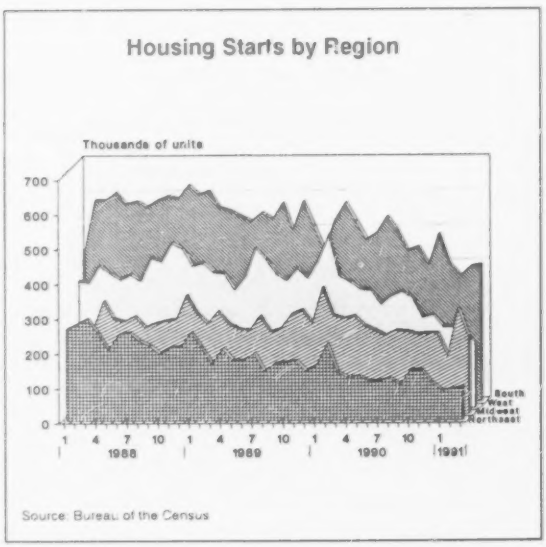
Regional Data

	Northeast	Midwest	South	West
Mar 1990	138	276	520	364
Nov 1990	147	232	483	268
Dec 1990	110	233	395	233
Jan 1991	86	167	361	233
Feb 1991	90	303	388	212
Mar 1991	***97***	***223***	***393***	***188***
Annual Averages:				
1989	181	269	535	397
1990	135	259	478	330
Percent Changes in March 1991 since:				
Mar 1990	-29.7	-19.2	-24.4	-48.4
Feb 1991	7.8	-26.4	1.3	-11.3

Source: Bureau of the Census, Construction Reports, Series C25



Source: Bureau of the Census, Real Estate Outlook forecast



Source: Bureau of the Census

After February's impressive performance, housing starts retreated in March, dropping 9.3 percent to an annual rate of 901,000 units. Weakness occurred in the construction of both single and multifamily structures. Starts of single-family homes fell 5.9 percent, to 732,000 units, while starts for multifamily homes fell 21.4 percent, to 169,000 units. While the March figures are disheartening, they remain above January's low figures.

March's decline was concentrated in two regions of the country. The Midwest, which led February's rally, accounted for most of the decline, decreasing 26.4 percent to an annual rate of 223,000 units. Weakness in the West also contributed to the decline, where starts fell 11.3 percent to 188,000 units. On a brighter note, the Northeast showed signs of stabilization, posting a 7.8 percent increase to 97,000 units. The South saw little change in activity from February to March, increasing a modest 1.3 percent, to 393,000 units.

Starts are expected to stabilize and regain strength in the months ahead. Single-family starts are projected to increase from an annual rate of 719,000 units in the first quarter of 1991 to 879,000 units by the end of the year. In the multifamily market, a tight lending environment will continue to limit construction activity in 1991. Starts will regain strength in the first half of 1992, and will increase at a healthy 26.4 percent in 1992. Single-family starts are projected to increase by 20.4 percent in 1992. Total housing starts are forecast to grow by 21.8 percent in 1992.

New Home Sales

(Seasonally Adjusted Annual Rates, in Thousands)

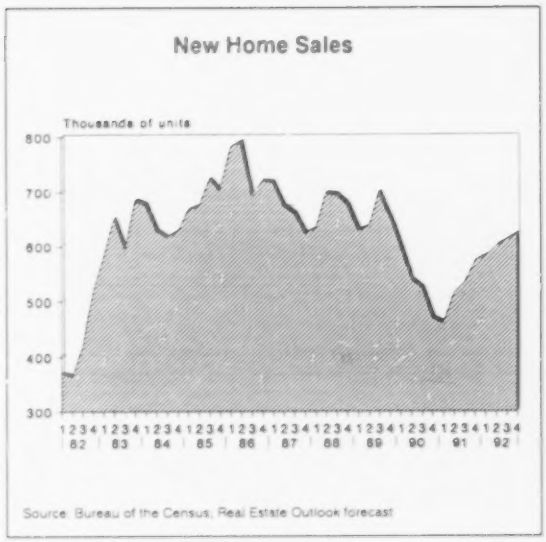
National Data

		Mo. Ago % Chg.	Yr. Ago % Chg.
Mar 1990	559	-7.8	0.5
Apr 1990	534	-4.5	-12.5
May 1990	535	0.2	-17.8
Jun 1990	549	2.6	-15.0
Jul 1990	541	-1.5	-27.0
Aug 1990	525	-3.0	-27.0
Sep 1990	504	-4.0	-21.0
Oct 1990	465	-7.7	-26.9
Nov 1990	480	3.2	-30.1
Dec 1990	464	-3.3	-26.7
Jan 1991	409	-11.9	-34.8
Feb 1991	485	18.6	-20.0
Mar 1991	***490***	***1.0***	***-12.3***
Annual Averages:			
1989	654		-3.1
1990	532		-18.5

Regional Data

	Northeast	Midwest	South	West
Mar 1990	84	94	221	160
Sep 1990	61	93	215	134
Oct 1990	74	70	209	113
Nov 1990	68	86	205	122
Dec 1990	62	86	195	121
Jan 1991	48	64	182	115
Feb 1991	53	106	199	127
Mar 1991	***47***	***90***	***197***	***155***
Annual Averages:				
1989	90	103	258	202
1990	74	90	223	146
Percent Changes in March 1991 since:				
Mar 1990	-44.0	-4.3	-10.9	-3.1
Feb 1991	-11.3	-15.1	-1.0	22.0

Source: Bureau of the Census, Construction Reports, Series C25



Source: Bureau of the Census; Real Estate Outlook forecast

Source: Bureau of the Census

Buoyed by vigorous activity in the Western region, new home sales rose for the second consecutive month this year. Total sales increased a modest one percent in March to an annual rate of 490,000 units. Following a large increase of 18.6 percent in February, March's sales increase is a sign of stability. The March figures support the view that January's dismal performance will be the nation's low point. A few key factors appear to be contributing to this recovery, notably lower mortgage rates and growing consumer confidence in the economy.

The West was the only region to record an increase in March, where sales grew by 22 percent to 155,000 units. After a spectacular gain of nearly 66 percent in February, sales in the Midwest declined by 15.1 percent to 90,000 units. Sales in the South fell by one percent, to 197,000 units. Still suffering from the effects of overexpansion in the real estate market, the Northeast saw sales decline by 11.3 percent to 47,000 units.

A recovery in the housing market is reflected in the forecast for new home sales. Favorable financing conditions, growing consumer confidence and pent-up demand will positively impact sales volume during the forecast period. New home sales are expected to rally as early as the second quarter of 1991, increasing 11.9 percent to an annual rate of 516,000 units. Sales are expected to grow at a healthy clip in 1991, increasing 3.5 percent and 7.3 percent in the third and fourth quarters of 1991, respectively. In 1992, sales will increase 15.9 to 604,000 units.

Existing Single-Family Home Sales

(Seasonally Adjusted Annual Rates, in Thousands)

National Data

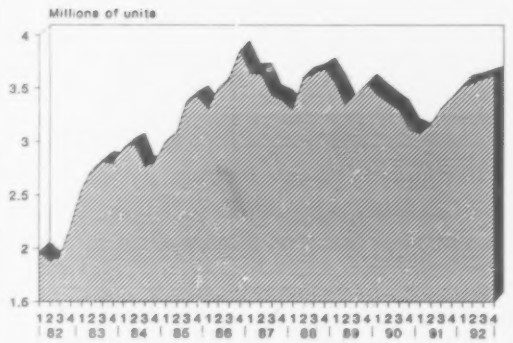
		Mo. Ago % Chg.	Yr. Ago % Chg.
Mar 1990	3,440	0.6	0.3
Apr 1990	3,370	-2.0	-2.0
May 1990	3,350	-0.6	3.1
Jun 1990	3,370	0.6	1.2
Jul 1990	3,320	-1.5	-1.8
Aug 1990	3,410	2.7	-0.9
Sep 1990	3,160	-7.3	-10.0
Oct 1990	3,070	-2.8	-12.0
Nov 1990	3,150	2.6	-11.5
Dec 1990	3,130	-0.6	-12.1
Jan 1991	2,900	-7.3	-16.4
Feb 1991	3,160	9.0	-7.6
Mar 1991	***3,180***	***0.6***	***-7.6***
Annual Averages:			
1989	3,440		-4.3
1990	3,296		-4.2

Regional Data

	Northeast	Midwest	South	West
Mar 1990	510	960	1,360	600
Oct 1990	500	820	1,240	500
Nov 1990	500	860	1,280	500
Dec 1990	500	880	1,260	490
Jan 1991	460	810	1,180	450
Feb 1991	500	880	1,240	540
Mar 1991	***520***	***970***	***1,150***	***530***
Annual Averages:				
1989	589	919	1,307	610
1990	522	892	1,325	557
Percent changes in March 1991 since:				
Mar 1990	2.0	1.0	-15.4	-11.7
Feb 1991	4.0	10.2	-7.3	-1.9

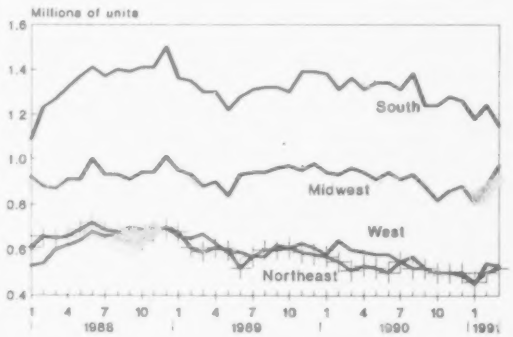
Source: National Association of Realtors,® "Home Sales"

Existing Home Sales



Source: NAR Economics & Research; Real Estate Outlook forecast

Existing Home Sales by Region



Source: NAR Economics & Research

After increasing 9 percent in February, sales of existing homes remained steady in March, increasing 0.6 percent to an annual rate of 3.18 million units. Activity in the lower price ranges dominated many markets, as favorable mortgage rates continued to draw buyers into the market and made homeownership more affordable to those with modest incomes.

By region, the Midwest and the Northeast recorded increases in sales, while the South and the West experienced declines. The Midwest, with its ample supply of moderately priced homes, had the largest gain, increasing 10.2 percent to 970,000 units. Sales rose for the second consecutive month in the Northeast, reaching 520,000 units, 4 percent above February's rate of 500,000 units. In the South, sales fell 7.3 percent to 1.15 million units. The West posted a resale rate of 530,000 units, down 1.9 percent from February's rate of 540,000 units.

As early as the the second quarter of 1991, sales are expected to rise, increasing 2.1 percent to 3.15 million units. By mid-summer, the full impact of favorable mortgage rates should be reflected in a noticeably larger volume of purchases. According to the NAR forecast, third quarter sales are projected to increase by 5 percent to an annual rate of 3.30 million units. Between the first and fourth quarters of 1991, sales are expected to increase by 331,000 units. The market will then be positioned for robust growth in 1992, when sales are expected to increase by 10.2 percent, to 3.56 million units.

Single-Family Home Prices

(In Dollars)

National Data

	Median		Average	
	Existing	New	Existing	New
Mar 1990	96,100	119,400	119,200	144,600
Oct 1990	92,900	120,000	115,900	153,000
Nov 1990	92,000	118,900	115,600	144,800
Dec 1990	91,700	127,000	114,100	153,400
Jan 1991	95,600	120,000	123,000	150,700
Feb 1991	94,000	120,000	119,700	150,500
Mar 1991	***96,500***	***125,000***	***122,500***	***163,400***
Annual Averages:				
1989	93,100	120,400	118,100	148,300
1990	95,500	122,300	118,600	149,100
Percent changes in March 1991 since:				
Mar 1990	0.4	4.7	2.8	13.0
Feb 1991	2.7	4.2	2.3	8.6

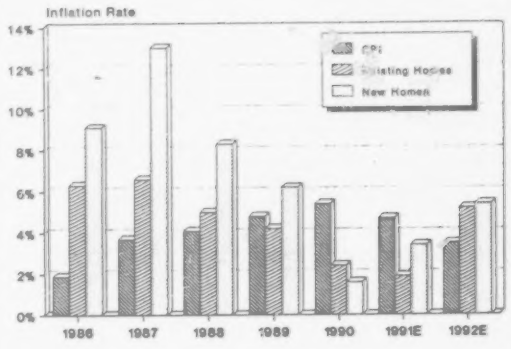
Regional Data

Median Prices for Existing Single-Family Homes

	Northeast	Midwest	South	West
Mar 1990	147,900	73,500	85,800	140,500
Oct 1990	136,200	72,000	83,200	142,000
Nov 1990	134,200	71,800	83,500	139,600
Dec 1990	134,400	72,300	82,800	131,400
Jan 1991	136,900	74,500	84,600	149,600
Feb 1991	137,200	76,400	83,200	137,100
Mar 1991	***142,300***	***76,200***	***87,500***	***137,600***
Annual Averages:				
1989	145,200	71,300	84,500	139,900
1990	141,200	74,000	85,900	139,600
Percent changes in March 1991 since:				
Mar 1990	-3.8	3.7	2.0	-2.1
Feb 1991	3.7	-0.3	5.2	0.4

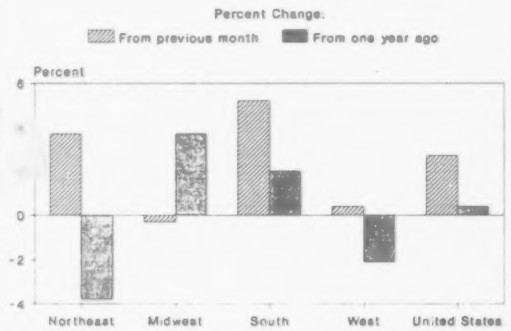
Source: National Association of Realtors,® "Home Sales"

Home Prices



Source: Bureau of the Census; E Real Estate Outlook forecast

Home Prices by Region



Source: NAR Economics & Research

The national median existing single-family home price increased to $96,500, 2.7 percent above February's median price of $94,000, and 0.4 percent above the median price recorded one year ago. In the market for new single-family homes, the median price increased 4.2 percent to $125,000 in March. Relative to one year ago, the median price of a new single-family home appreciated 4.7 percent.

The average price of an existing single-family home increased by 2.3 percent in March to $122,500. Since March of 1990, the average price has risen 2.8 percent. The average price of a new single-family home increased to $163,400 in March, 8.6 percent above February's median price of $150,500.

Modest appreciation in the median price of existing single-family homes is expected over the next year, with an overall increase of 1.9 percent in 1991. Prices will begin to firm at the beginning of 1992, and are projected to increase 5.2 percent in that year. New single-family home prices should experience strong appreciation in 1991, with prices projected to increase by 3.4 percent. In 1992 the median price of a new single-family home is projected to increase by 5.4 percent.

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The Payoffs and Risks of Easing Monetary Policy:

Results of a Model-Based Simulation

The Federal Reserve has come under pressure from many sides to ease monetary policy in order to revitalize the economy and end the recession. The Administration has publicly suggested that the Fed has not gone far enough in easing credit, and even Fed Chairman Alan Greenspan is known to have favored moving more aggressively against the recession earlier this spring. His view turned out to be in the minority among the Fed policymakers at the time, and further easing was delayed.

This article does not seek to suggest that the Fed should ease rates further today, although many have made that case. Rather, the point of this article is to show the tradeoffs the Fed faces in deciding whether to ease monetary policy another notch or whether to hold fast. By using an econometric model of the U.S. economy, we will uncover some of the shifts that can result from a change in credit policy. We will use a ten-year simulation of the economy to judge its impact on measures such as GNP growth, unemployment, inflation, and housing starts.

The following section presents the Fed's overall objectives in setting monetary policy. This is followed by a simplified overview of the mechanics of putting the new policy in place and a section on the dangers of easing too much. Before looking at the results of the simulation, we'll briefly describe how the Federal Reserve has responded during the current recession.

The Name of the Game

The Fed's goal is to promote long-term, noninflationary economic growth. Over the long term, providing growth and price stability are not incompatible; in fact, real price stability, as opposed to low inflation, would boost strong economic growth. In the short-term, however, there is a trade-off between growth and inflation. We can have greater growth today at the cost of higher inflation later, or we can slow economic growth now for the rewards of lower inflation later. The Fed took the latter course in the late 1980s under its so-called soft landing policy. Today the Fed must determine how to alter monetary policy so that economic recovery is encouraged without setting the stage for greater inflation later.

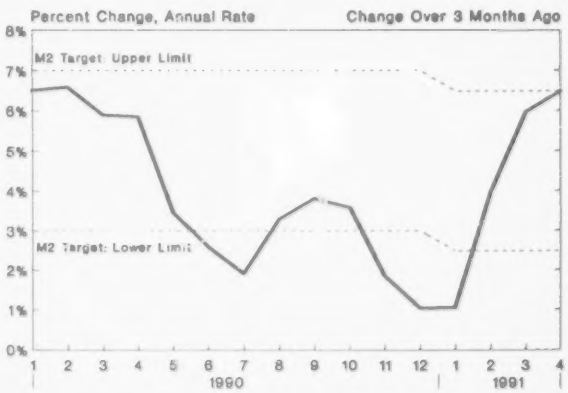
How The Game Is Played

Although the Federal Reserve is often exhorted to lower interest rates, it doesn't set any market interest rates, strictly speaking. It does set the discount rate, but that's only for borrowing between the Fed and individual banks. The market interest rate most affected by the Fed is the rate that's charged for overnight loans between banks. Known as the fed funds rate, it moves in response to supply and demand conditions among banks as they seek to cover their reserve requirements. The Fed influences the fed funds rate to move toward the target it has set by affecting reserve availability.

In easing monetary policy, the Fed supplies more reserves to the banking system. With a greater supply of reserves on hand, and everything else being equal, the fed funds rate drops. Banks have more funds to loan out, and, so the story goes, more loans are made to fuel economic activity. In a competitive marketplace, loan rates for consumer and business lending fall. Businesses are more likely to borrow funds for expansion, and consumers are more likely to borrow to buy new cars, new homes, vacations, appliances, and so forth. This stimulation of demand means more products are required, and so employment and incomes rise as well.

Time is required for the Fed's easing to work through the economy, and it may be months after the fact before the Fed learns the impact of their policy change. One early signal is thought to be the money supply, since the new loans are generally funneled through checking accounts, which are part of the money supply. Consequently, growth in the money supply is seen as an indicator of economic activity. Recent growth in the money supply measure known as M2 is pictured below, and the below-target growth in late 1990 led many to feel that the Fed

Money Supply Growth Bounces Back



needed to ease further. Growth has rebounded in recent months, and some may take this as a signal that the credit easing of earlier months is passing through the system.

The Risk of Easing Too Much

With the benefit of stronger economic growth, why doesn't the Fed simply ease? There is a serious downside to a monetary policy that's too loose: inflation. With the extra credit available, consumers and businesses begin demanding more goods and services before suppliers have produced them. If the money has been created too quickly, then demand outstrips supply and, in a competitive marketplace, the increased demand causes prices to rise. Eventually, the rising prices lead workers to seek higher wage and salary increases, and this in turn leads to higher costs for suppliers. An inflationary cycle has been kicked off, with the result that suppliers, after initially boosting production, begin to cut back output. Concerned about high inflation, the monetary authorities then scale back credit availability, interest rates rise, and demand cools off. As it turns out, the seed of the boom-bust cycle is usually poorly-handled monetary policy.

To avoid an inflationary cycle (or a deflationary episode such as the Great Depression), the increase in money created by the Fed must match the growth in the output of goods and services in the economy. In other words, the source of new wealth in the economy is increased production, not the creation of new money by the Federal Reserve.

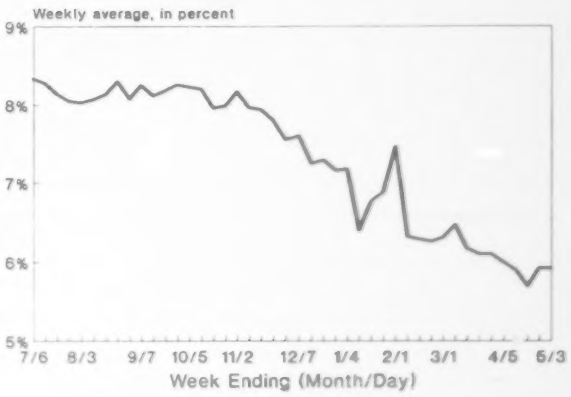
While discussing the nature of inflation, it's worth pointing out that there is no one rate of inflation, and its impact is not uniform on the various sectors of the economy. Because inflation affects manufacturing differently than services, for example, it distorts the judgement of the true cost of one activity relative to another. It's the price system that coordinates economic activity in a free market, and the additional static inflation adds to the transmission of prices throughout the economy is costly.

What The Fed Has Done So Far In This Recession

The fed funds rate hovered around 8.25 percent during the first half of 1990. This was about 2 percentage points higher than it was in early 1988, when the Fed launched its soft-landing initiative in order to lower inflation. After detecting the discomfort of the credit crunch in some areas, the Fed lowered its fed funds target rate to 8 percent in July. In October, at the conclusion of the federal budget negotiations, another one-quarter point drop in the target was announced. Since then, as the weakness in the economy grew increasingly evident, the Fed has increased reserve availability such that the fed funds rate is currently averaging just under 6 percent. In addition, the Fed eliminated some reserve requirements in December, which also released loanable funds to the banking system.

Now the question is: Having eased this much over the past 10 months or so, should the Fed sit tight and let its monetary tonic take effect? Or, in light of the credit crunch and the lack of a vibrant sector that could lead us out of recession, should the Fed ease further?

The Fall in the Fed Funds Rate

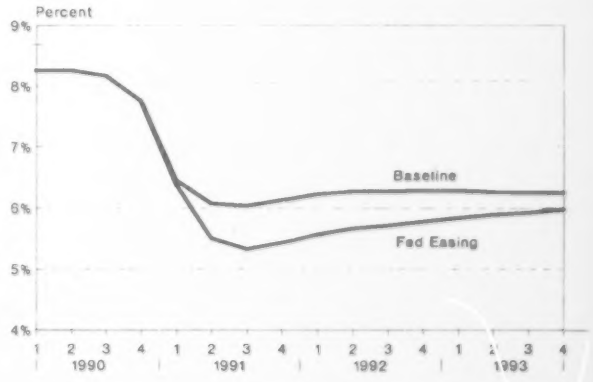


The Simulation Results

By now we've set the stage to discuss the model simulation. The first step was to develop a baseline case, against which we can compare the results of the experiment. To show the full, long-term effects of the Federal Reserve's actions, a projection was prepared using a ten-year forecast horizon, which allows the economic effects enough time to work their way through the economy. The first three years of the forecast, 1991-93, replicate NAR's April forecast, and the remaining seven years show an economy growing close to its long-term trend.

An alternative projection was prepared to compare

The Simulation Experiment: The Change in the Federal Funds Rate



Simulation Results for Selected Variables

	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000
Real GNP Growth											
percent change											
Baseline	1.0	-0.2	2.9	2.8	2.1	2.5	3.1	2.9	3.1	2.4	2.2
Fed Easing	1.0	0.0	3.6	3.4	2.0	2.0	2.6	2.3	2.7	2.6	2.4
Unemployment Rate											
percent											
Baseline	5.5	6.8	6.4	5.9	6.0	6.1	5.8	5.7	5.5	5.5	5.7
Fed Easing	5.5	6.7	6.0	5.3	5.5	5.8	5.8	6.0	6.0	6.0	6.1
Consumer Prices											
percent change											
Baseline	5.4	4.4	3.4	3.5	2.8	3.1	3.0	2.9	2.9	2.9	2.9
Fed Easing	5.4	4.4	3.5	4.0	3.5	3.9	3.7	3.4	3.1	2.9	2.7
Short-Term Interest Rates											
percent											
Baseline	7.5	5.9	5.8	5.8	5.3	5.3	5.3	5.2	5.2	5.0	4.9
Fed Easing	7.5	5.4	5.3	5.5	5.2	5.2	5.2	5.1	5.1	5.0	4.8
Long-Term Interest Rates											
percent											
Baseline	8.6	8.1	7.8	7.6	7.1	6.9	6.8	6.7	6.7	6.6	6.4
Fed Easing	8.6	7.9	7.5	7.3	6.8	6.7	6.7	6.6	6.6	6.5	6.4
Mortgage Rates											
percent											
Baseline	10.1	9.2	8.9	8.8	8.2	8.0	7.9	7.8	7.8	7.7	7.5
Fed Easing	10.1	9.0	8.5	8.5	7.9	7.8	7.8	7.7	7.7	7.6	7.4
Housing Starts											
thousands of units											
Baseline	1,202	1,055	1,266	1,342	1,351	1,395	1,427	1,385	1,314	1,230	1,233
Fed Easing	1,202	1,080	1,325	1,378	1,346	1,386	1,403	1,343	1,277	1,213	1,206

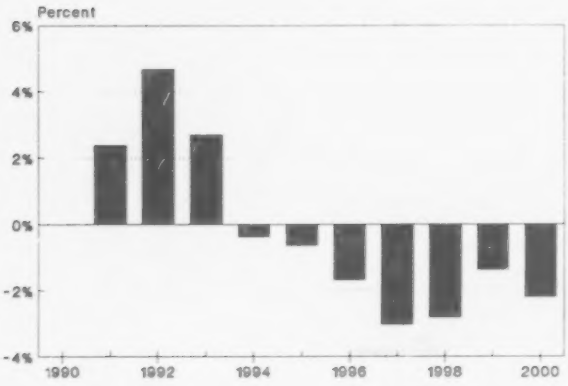
with the baseline simulation. In the alternative, credit growth is expanded enough to cause the fed funds rate to fall from about 6 percent to about 5.5 percent for two quarters in 1991. Growth in credit is then brought up gradually to the same rate so that by 1993 and beyond the growth assumptions in the two simulations are identical (see the chart comparing the two fed funds rates). Consequently, the only difference in the assumptions underlying the two simulations is this ease in credit policy in 1991-92. All of the changes in the other variables, as presented in the table, result from this difference of assumptions.

A more aggressive easing assumption would have magnified the differences between the two simulations, but a half-point decline in the fed funds rate was chosen since it is a reasonable alternative for the Fed to consider in today's situation and still produces measurable differences between the two simulations.

A look at several key variables will illustrate the tradeoffs the Fed faces as it considers easing monetary policy:

Real GNP: As expected, the Fed easing produces stronger growth in the short run. Total production in the economy, measured in after-inflation dollars, is up 3.6 percent in 1992 in the easing scenario; in the baseline projection, real GNP rises 2.9 percent. By 1993, goods and services valued at an extra $66.9 billion have been produced. But the gap between the two simulations shrinks after 1993, and, as the economy grapples with higher inflation, output growth in the easing scenario declines below that of the baseline. By the year 2000, the

A Wash in the Long-Run:
The Difference in Housing Starts



economy is at virtually the same spot in the two simulations: $5,256 billion in the base case, $5,252 billion in the easing case, a difference of less than one-tenth of one percentage point.

Unemployment Rate: Following the lead of GNP, the unemployment rate improves in the first three years of the simulation relative to the baseline, falling to the pre-recession level of 5.3 percent in 1993. But again, economic performance has been hampered in the later years, and the gap between the two unemployment rates closes by 1996. In the final four years, the rate in the easing scenario exceeds that of the baseline case.

Consumer Price Index: The cost of greater output in the short-run is apparent in the comparison between the rates of inflation. For seven consecutive years, the CPI grows faster in the easing simulation than it does in the baseline case.

Interest Rates on Government Securities: The short-term interest rate (in this case the 3-month Treasury Bill) is more responsive to the Fed's easing, falling a half-percentage point immediately in 1991. The long-term rate (30-year Treasury Bond) falls as well, but only by three-tenths of a point at its widest. In both cases the gap between the two simulations narrows over time.

Housing Market: Mortgage rates fall faster in the easing scenario, and the rebound in the housing market is consequently stronger. In 1992, housing starts in the easing case are higher by 59,000 units, or almost 5 percent (see chart). After the first three years of the simulation, the advantage swings over to the baseline scenario. In the ten years of the simulation, housing starts totaled 12,998,000 units in the base case and 12,957,000 units in the alternative case, a difference over ten years of 41,000 units, or three-tenths of one percent.

Another alternative is for the Fed to ease now, but, beginning in 1993, tighten credit policy further than we have assumed in our simulation. This action would be designed to choke off the extra inflation induced by the easing of the early 1990s. However, because of monetary policy's time lag and the difficulty in pinpointing our present position and course, such fine-tuning is extremely difficult. The tools the Fed has to work with are crude, not precise, and the economy is as nimble at changing course as an ocean liner.

Conclusion

The answer for the Fed is not obvious, and it may rest on the assumptions made about the economy's initial conditions. In our scenario, the economy is assumed to post a marginally positive growth rate in the second quarter of 1991, with the first quarter of solid growth coming in the following quarter. If we're wrong, and the economy continues to decline significantly in the second and third quarters of 1991, then we may wish the Fed had eased more today. On the other hand, if the economy is able to shake off its slumber sooner than expected and robust growth returns in the second quarter, we may be glad that the Fed didn't go further in easing credit policy. Stoking the credit furnace up too much may, by the time the fire spreads, produce too much inflationary heat later.

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Forecasting & Policy Analysis

Note: Simulations were run on the Laurence H. Meyer & Associates' model of the U.S. economy.

These historical tables are a new feature
and will appear in the February, May, August and November
issues of the Real Estate Outlook.

Economic Indicators

	GNP	CPI	Unemployment Rate	Mortgage Rate	Short-Term Rate	Long-Term Rate
	Percent Change	*Percent Change*	*Percent*	*Percent*	*Percent*	*Percent*
Annual						
1980	-0.2	13.5	7.2	13.8	11.4	11.3
1981	1.9	10.4	5.8	10.6	9.4	9.0
1982	-2.5	6.2	6.4	12.9	11.1	10.3
1983	3.6	3.2	9.6	13.2	8.6	11.2
1984	6.8	4.4	7.5	13.9	9.5	12.4
1985	3.4	3.5	7.2	12.4	7.5	10.8
1986	2.7	1.9	7.0	10.2	6.0	7.8
1987	3.4	3.7	6.2	10.2	5.8	8.6
1988	4.5	4.1	5.5	10.3	6.7	9.0
1989	2.5	4.8	5.3	10.3	8.1	8.4
1990	1.0	5.4	5.5	10.1	7.5	8.6
Quarterly						
1984:1	10.7	5.8	7.9	13.3	9.2	12.0
2	5.5	3.8	7.4	14.0	9.8	13.2
3	2.6	3.5	7.4	14.5	10.3	12.7
4	1.7	3.5	7.3	13.7	8.8	11.7
1985:1	4.9	3.7	7.2	13.1	8.2	11.6
2	2.4	3.7	7.3	12.8	7.5	11.0
3	4.1	2.5	7.2	12.1	7.1	10.6
4	3.0	4.1	7.0	11.7	7.2	10.0
1986:1	6.6	2.1	7.0	10.6	6.9	8.8
2	-1.8	-1.9	7.2	10.3	6.1	7.5
3	0.8	2.5	7.0	10.2	5.5	7.4
4	2.3	2.8	6.8	9.7	5.4	7.5
1987:1	5.2	5.4	6.6	9.1	5.5	7.5
2	4.2	4.6	6.3	10.3	5.7	8.5
3	4.1	4.1	6.0	10.5	6.0	9.1
4	6.6	3.8	5.8	10.9	5.9	9.2
1988:1	5.1	3.2	5.7	10.1	5.7	8.6
2	3.6	4.7	5.5	10.4	6.2	9.1
3	2.7	5.2	5.5	10.5	7.0	9.2
4	2.7	4.3	5.3	10.4	7.7	9.0
1989:1	3.6	5.0	5.2	10.8	8.5	9.0
2	1.6	6.2	5.3	10.7	8.4	8.7
3	1.7	3.2	5.3	10.0	7.8	8.1
4	0.3	4.0	5.3	9.8	7.7	7.9
1990:1	1.7	7.4	5.3	10.1	7.8	8.4
2	0.4	3.9	5.3	10.3	7.7	8.7
3	1.4	6.9	5.6	10.1	7.5	8.8
4	-1.6	7.0	5.9	10.0	7.0	8.5
1991:1	-2.8	3.5	6.5	9.5	6.0	8.2

Note: Quarterly levels and percentages are annualized. Quarterly figures may not average to annual figures due to rounding. The 3-Month Treasury Bill is shown as "Short-Term Rate"; The 30-Year Treasury Bond is shown as "Long-Term Rate."

Housing Starts

Thousands of Units, Seasonally Adjusted; Percent Change

	Total		Single-Family		Multi-Family	
Annual						
1980	1,300	-24.3	855	-27.0	445	-18.4
1981	1,096	-15.7	711	-16.9	386	-13.4
1982	1,057	-3.6	663	-6.7	394	2.3
1983	1,705	61.3	1,065	60.6	641	62.4
1984	1,768	3.7	1,098	3.1	669	4.5
1985	1,741	-1.5	1,071	-2.5	671	0.2
1986	1,812	4.0	1,182	10.4	630	-6.1
1987	1,631	-10.0	1,154	-2.4	476	-24.3
1988	1,488	-8.7	1,083	-6.2	405	-15.0
1989	1,381	-7.2	1,005	-7.2	376	-7.2
1990	1,203	-12.9	901	-10.4	302	-19.7
Quarterly						
1984:1	1,940	12.2	1,221	16.0	719	6.3
2	1,829	-5.7	1,103	-9.6	726	1.0
3	1,671	-8.7	1,004	-9.0	667	-8.1
4	1,630	-2.4	1,066	6.2	565	-15.4
1985:1	1,714	5.2	1,064	-0.2	650	15.2
2	1,726	0.7	1,053	-1.0	673	3.4
3	1,701	-1.4	1,059	0.6	642	-4.6
4	1,825	7.3	1,108	4.6	717	11.7
1986:1	1,899	4.1	1,198	8.1	701	-2.2
2	1,878	-1.1	1,215	1.5	663	-5.5
3	1,759	-6.4	1,161	-4.4	597	-9.9
4	1,712	-2.6	1,155	-0.5	557	-6.8
1987:1	1,761	2.9	1,237	7.1	524	-5.9
2	1,612	-8.5	1,138	-8.0	474	-9.6
3	1,625	0.8	1,163	2.2	462	-2.5
4	1,524	-6.2	1,079	-7.3	445	-3.7
1988:1	1,425	-6.5	1,057	-2.0	368	-17.2
2	1,491	4.6	1,066	0.9	425	15.3
3	1,484	-0.4	1,071	0.5	413	-2.8
4	1,551	4.5	1,137	6.1	414	0.4
1989:1	1,464	-5.6	1,026	-9.8	438	5.8
2	1,360	-7.1	999	-2.7	362	-17.5
3	1,348	-0.9	1,003	0.4	346	-4.4
4	1,352	0.2	994	-0.9	358	3.5
1990:1	1,433	6.0	1,064	7.1	369	3.2
2	1,204	-16.0	896	-15.8	308	-16.5
3	1,131	-6.1	856	-4.4	274	-10.9
4	1,042	-7.8	786	-8.2	256	-6.7
1991:1	937	-10.1	726	-7.7	211	-17.4

Note: Quarterly levels are annualized. Simple percent changes are shown.
Quarterly figures may not average to annual figures due to rounding.

Housing Starts by Region

Thousands of Units, Seasonally Adjusted; Percent Change

	Northeast		Midwest		South		West	
Annual								
1980	125	-30.9	218	-34.0	647	-12.6	309	-33.4
1981	117	-6.5	175	-19.7	565	-12.7	239	-22.8
1982	113	-3.2	142	-18.8	596	5.4	206	-13.7
1983	171	50.8	217	52.8	937	57.3	380	84.5
1984	207	20.7	247	13.6	873	-6.8	440	15.7
1985	249	20.8	237	-4.0	785	-10.1	470	6.8
1986	298	19.5	298	25.8	732	-6.8	484	3.0
1987	269	-9.7	308	3.3	633	-13.5	420	-13.1
1988	239	-11.4	272	-11.9	574	-9.3	404	-3.9
1989	181	-24.1	269	-1.1	535	-6.7	397	-1.9
1990	135	-25.2	259	-3.7	478	-10.6	330	-16.7
Quarterly								
1984:1	201	29.4	269	29.1	976	0.8	494	24.2
2	197	-1.8	252	-6.2	922	-5.5	451	-8.7
3	195	-1.4	233	-7.7	825	-10.6	420	-6.9
4	233	19.7	234	0.3	768	-6.8	395	-5.8
1985:1	228	-2.3	222	-4.9	790	2.8	474	20.0
2	260	14.3	243	9.1	765	-3.1	457	-3.6
3	230	-11.7	236	-2.9	755	-1.4	481	5.1
4	280	21.6	248	5.2	830	10.0	467	-2.8
1986:1	315	12.6	294	18.5	809	-2.5	481	2.9
2	290	-7.9	298	1.5	776	-4.1	514	6.9
3	299	3.1	302	1.1	706	-9.0	452	-12.0
4	288	-3.7	300	-0.7	636	-9.9	489	8.1
1987:1	285	-0.9	372	24.1	633	-0.5	471	-3.5
2	273	-4.3	296	-20.3	631	-0.3	412	-12.7
3	265	-3.1	281	-5.1	658	4.3	421	2.3
4	254	-4.2	283	0.7	609	-7.4	377	-10.4
1988:1	278	9.7	235	-17.1	532	-12.6	380	0.6
2	236	-15.1	290	23.4	583	9.5	382	0.5
3	234	-1.1	266	-8.4	578	-0.9	407	6.6
4	206	-12.0	296	11.3	602	4.2	448	10.1
1989:1	211	2.4	283	-4.2	571	-5.1	399	-10.9
2	185	-12.2	250	-11.8	532	-6.8	393	-1.5
3	168	-9.4	256	2.5	531	-0.3	393	0.1
4	161	-4.2	284	10.9	506	-4.7	401	1.9
1990:1	172	7.3	308	8.4	538	6.3	415	3.5
2	122	-29.2	260	-15.8	495	-8.0	327	-21.1
3	114	-6.8	235	-9.5	457	-7.7	325	-0.7
4	134	17.6	232	-1.4	423	-7.4	254	-21.9
1991:1	91	-31.9	231	-0.3	381	-10.1	211	-16.8

Note: Quarterly levels are annualized. Simple percent changes are shown.
Quarterly figures may not average to annual figures due to rounding.

New Home Sales

Thousands of Units, Seasonally Adjusted; Percent Change

	U.S.		Northeast		Midwest		South		West	
Annual										
1980	545	-22.5	51	-25.6	81	-27.3	269	-11.1	145	-34.8
1981	436	-20.1	46	-8.4	60	-26.1	218	-18.9	112	-23.1
1982	418	-4.0	47	2.0	48	-20.1	223	2.3	100	-10.0
1983	627	50.0	76	61.1	71	48.9	328	47.0	152	51.7
1984	637	1.5	90	18.8	76	7.0	310	-5.5	161	5.4
1985	691	8.6	110	22.0	82	8.1	325	4.9	174	8.4
1986	746	8.0	134	21.4	95	15.5	320	-1.6	197	13.5
1987	669	-10.4	117	-12.7	97	2.5	269	-16.0	186	-5.9
1988	675	0.9	101	-13.8	98	0.1	271	0.7	206	10.6
1989	654	-3.1	90	-10.8	103	6.1	258	-4.8	202	-1.7
1990	532	-18.5	74	-17.6	90	-13.5	223	-13.7	146	-27.6
Quarterly										
1984:1	676	-1.0	86	12.7	76	0.4	336	-9.1	179	10.7
2	628	-7.1	86	0.8	79	3.9	301	-10.3	162	-9.7
3	616	-1.9	99	15.1	74	-6.3	302	0.3	140	-13.2
4	627	1.8	90	-9.7	75	1.8	301	-0.2	161	14.7
1985:1	666	6.2	100	11.9	85	12.8	320	6.3	160	-0.4
2	673	1.1	104	3.3	79	-7.5	323	0.9	168	4.6
3	723	7.4	117	13.2	84	7.2	333	3.0	189	12.5
4	703	-2.8	119	1.4	81	-4.0	325	-2.5	179	-5.1
1986:1	780	11.0	138	16.2	89	10.3	349	7.4	204	13.8
2	791	1.4	142	2.4	99	10.8	336	-3.5	215	5.4
3	694	-12.3	123	-13.4	90	-8.8	299	-11.2	182	-15.2
4	720	3.7	132	7.6	101	12.2	297	-0.4	189	4.0
1987:1	718	-0.3	126	-4.8	106	4.9	293	-1.3	192	1.6
2	674	-6.1	108	-13.8	100	-6.3	278	-5.1	188	-2.4
3	660	-2.1	118	8.9	87	-12.4	271	-2.6	184	-1.8
4	623	-5.6	115	-2.5	96	10.3	234	-13.8	179	-2.9
1988:1	632	1.4	105	-8.7	96	0.0	255	9.1	176	-1.7
2	697	10.2	111	5.4	94	-2.1	287	12.4	205	16.3
3	695	-0.3	97	-12.0	97	2.5	279	-2.6	221	8.1
4	676	-2.7	90	-7.9	103	6.2	263	-5.7	220	-0.5
1989:1	628	-7.1	102	13.4	103	0.0	237	-9.9	186	-15.6
2	636	1.3	81	-20.3	99	-3.6	257	8.4	198	6.5
3	699	10.0	84	4.1	110	10.8	278	8.2	226	14.3
4	652	-6.8	92	9.1	102	-6.7	260	-6.7	198	-12.7
1990:1	597	-8.4	84	-9.1	95	-7.5	240	-7.4	179	-9.6
2	539	-9.7	79	-6.0	92	-3.2	219	-8.9	150	-15.9
3	523	-3.0	65	-16.9	91	-0.7	229	4.7	137	-8.6
4	470	-10.3	68	4.1	81	-11.4	203	-11.5	119	-13.6
1991:1	461	-1.8	49	-27.5	87	7.4	193	-5.1	132	11.5

Note: Quarterly levels are annualized. Simple percent changes are shown.
Quarterly figures may not average to annual figures due to rounding.

Existing Home Sales

Thousands of Units, Seasonally Adjusted; Percent Change

	U.S.		Northeast		Midwest		South		West	
Annual										
1980	2,973	-22.3	403	-23.4	806	-24.0	1,092	-19.3	672	-24.2
1981	2,419	-18.6	353	-12.4	632	-21.6	917	-16.0	516	-23.2
1982	1,990	-17.7	354	0.3	490	-22.5	780	-14.9	366	-29.1
1983	2,719	36.6	493	39.3	709	44.7	1,035	32.7	481	31.4
1984	2,868	5.5	511	3.7	755	6.5	1,073	3.7	529	10.0
1985	3,214	12.1	622	21.7	866	14.7	1,172	9.2	554	4.7
1986	3,565	10.9	703	13.1	991	14.4	1,261	7.6	610	10.1
1987	3,526	-1.1	685	-2.6	959	-3.2	1,282	1.7	600	-1.6
1988	3,594	1.9	673	-1.8	929	-3.1	1,350	5.3	642	7.0
1989	3,440	-4.3	589	-12.5	919	-1.1	1,307	-3.2	610	-5.0
1990	3,296	-4.2	522	-11.4	892	-2.9	1,325	1.4	557	-8.7
Quarterly										
1984:1	2,927	4.8	500	0.0	783	10.8	1,103	2.2	540	7.3
2	2,983	1.9	523	4.7	777	-0.9	1,123	1.8	557	3.1
3	2,763	-7.4	510	-2.5	723	-6.9	1,027	-8.6	507	-9.0
4	2,800	1.3	507	-0.7	737	1.8	1,040	1.3	510	0.7
1985:1	2,993	6.9	560	10.5	783	6.3	1,127	8.3	530	3.9
2	3,070	2.6	583	4.2	823	5.1	1,123	-0.3	543	2.5
3	3,370	9.8	657	12.6	933	13.4	1,217	8.3	563	3.7
4	3,423	1.6	683	4.1	930	-0.4	1,227	0.8	580	3.0
1986:1	3,340	-2.4	683	0.0	927	-0.4	1,167	-4.9	557	-4.0
2	3,493	4.6	690	1.0	1,013	9.4	1,213	4.0	583	4.8
3	3,593	2.9	693	0.5	990	-2.3	1,293	6.6	617	5.7
4	3,833	6.7	747	7.7	1,033	4.4	1,377	6.4	680	10.3
1987:1	3,693	-3.7	713	-4.5	1,077	4.2	1,300	-5.6	607	-10.6
2	3,613	-2.2	697	-2.3	977	-9.3	1,317	1.3	623	2.7
3	3,427	-5.2	677	-2.9	900	-7.8	1,263	-4.1	587	-5.9
4	3,333	-2.7	653	-3.4	887	-1.5	1,233	-2.4	567	-3.4
1988:1	3,297	-1.1	643	-1.5	890	0.4	1,207	-2.2	557	-1.8
2	3,600	9.2	683	6.2	933	4.9	1,350	11.9	630	13.2
3	3,630	0.8	673	-1.5	933	0.0	1,360	0.7	660	4.8
4	3,690	1.7	660	-2.0	953	2.1	1,410	3.7	663	0.5
1989:1	3,547	-3.9	627	-5.1	920	-3.5	1,337	-5.2	660	-0.5
2	3,340	-5.8	577	-8.0	890	-3.3	1,267	-5.2	603	-8.6
3	3,443	3.1	590	2.3	947	6.4	1,317	3.9	587	-2.8
4	3,537	2.7	593	0.6	967	2.1	1,360	3.3	617	5.1
1990:1	3,443	-2.6	543	-8.4	943	-2.4	1,350	-0.7	607	-1.6
2	3,363	-2.3	517	-4.9	930	-1.4	1,330	-1.5	583	-3.8
3	3,297	-2.0	530	2.6	907	-2.5	1,310	-1.5	547	-6.3
4	3,117	-5.5	500	-5.7	853	-5.9	1,260	-3.8	497	-9.1
1991:1	3,080	-1.2	493	-1.3	887	3.9	1,190	-5.6	507	2.0

Note: Quarterly levels are annualized. Simple percent changes are shown.
Quarterly figures may not average to annual figures due to rounding.

Existing Home Prices

Dollars

	U.S.		Northeast		Midwest		South		West	
Annual										
1980	62,200	12.0	60,800	14.1	51,900	8.8	58,300	13.9	89,300	15.0
1981	66,400	6.8	63,700	4.8	54,300	4.6	64,400	10.5	96,200	7.7
1982	67,800	2.1	63,500	-0.3	55,100	1.5	67,100	4.2	98,900	2.8
1983	70,300	3.7	72,200	13.7	56,600	2.7	69,200	3.1	94,900	-4.0
1984	72,400	3.0	78,700	9.0	57,100	0.9	71,300	3.0	95,800	0.9
1985	75,500	4.3	88,900	13.0	58,900	3.2	75,200	5.5	95,400	-0.4
1986	80,300	6.4	104,800	17.9	63,500	7.8	78,200	4.0	100,900	5.8
1987	85,600	6.6	133,300	27.2	66,000	3.9	80,400	2.8	113,200	12.2
1988	89,300	4.3	143,000	7.3	68,400	3.6	82,200	2.2	124,900	10.3
1989	93,100	4.3	145,200	1.5	71,300	4.2	84,500	2.8	139,900	12.0
1990	95,500	2.6	141,200	-2.8	74,000	3.8	85,900	1.7	139,600	-0.2
Quarterly										
1984:1	71,300	1.8	75,267	3.7	57,200	3.2	70,133	1.3	96,467	1.8
2	72,733	2.0	77,667	3.2	58,133	1.6	71,967	2.6	96,033	-0.4
3	73,200	0.6	80,133	3.2	57,167	-1.7	72,033	0.1	95,867	-0.2
4	71,967	-1.7	81,733	2.0	55,267	-3.3	70,833	-1.7	94,900	-1.0
1985:1	74,133	3.0	86,267	5.5	58,367	5.6	73,533	3.8	93,500	-1.5
2	75,500	1.8	88,333	2.4	59,400	1.8	75,200	2.3	94,567	1.1
3	76,600	1.5	89,467	1.3	59,400	0.0	76,767	2.1	97,367	3.0
4	75,200	-1.8	91,300	2.0	58,100	-2.2	74,533	-2.9	95,700	-1.7
1986:1	78,100	3.9	98,867	8.3	62,167	7.0	77,433	3.9	95,700	0.0
2	82,000	5.0	106,567	7.8	65,333	5.1	80,433	3.9	101,433	6.0
3	80,733	-1.5	106,033	-0.5	63,567	-2.7	78,233	-2.7	101,567	0.1
4	80,200	-0.7	107,233	1.1	62,433	-1.8	75,867	-3.0	101,533	-0.0
1987:1	84,567	5.4	124,467	16.1	66,967	7.3	80,933	6.7	106,867	5.3
2	85,967	1.7	134,400	8.0	66,433	-0.8	81,567	0.8	111,933	4.7
3	86,767	0.9	138,167	2.8	66,200	-0.4	80,433	-1.4	116,567	4.1
4	85,000	-2.0	134,700	-2.5	64,400	-2.7	79,367	-1.3	116,533	-0.0
1988:1	88,633	4.3	138,267	2.6	67,433	4.7	82,800	4.3	119,367	2.4
2	89,267	0.7	144,133	4.2	68,867	2.1	83,033	0.3	122,600	2.7
3	90,233	1.1	144,867	0.5	68,900	0.0	83,167	0.2	126,833	3.5
4	88,700	-1.7	142,700	-1.5	67,700	-1.7	79,700	-4.2	129,867	2.4
1989:1	91,167	2.8	143,400	0.5	69,367	2.5	84,067	5.5	133,633	2.9
2	93,000	2.0	145,833	1.7	70,900	2.2	84,867	1.0	139,400	4.3
3	94,933	2.1	147,067	0.8	72,500	2.3	85,733	1.0	145,300	4.2
4	92,667	-2.4	144,100	-2.0	71,833	-0.9	82,833	-3.4	140,867	-3.1
1990:1	95,467	3.0	144,900	0.6	73,167	1.9	85,433	3.1	143,367	1.8
2	96,600	1.2	143,500	-1.0	74,633	2.0	86,767	1.6	139,433	-2.7
3	96,567	-0.0	141,900	-1.1	75,133	0.7	87,300	0.6	138,200	-0.9
4	92,200	-4.5	134,933	-4.9	72,033	-4.1	83,167	-4.7	137,667	-0.4
1991:1	95,367	3.4	138,800	2.9	75,700	5.1	85,100	2.3	141,433	2.7

Note: Quarterly levels are annualized. Simple percent changes are shown.
Quarterly figures may not average to annual figures due to rounding.

U.S. Economic Outlook: May 1991

Quarterly figures are seasonally adjusted annual rates

	90.4	91.1	91.2	91.3	91.4	92.1	92.2	92.3	1989	1990	1991	1992	1993
U.S. Economy													
Annual Growth Rate													
Real GNP	-1.6	-2.8	-0.2	2.1	2.7	3.6	3.2	2.9	2.5	1.0	-0.4	2.8	2.8
Industrial Production	-7.2	-9.2	-2.1	2.7	4.3	5.4	5.3	5.2	2.6	1.0	-2.8	4.3	4.9
Civilian Employment	-0.9	-2.4	-0.5	0.6	0.5	0.8	1.1	1.4	2.0	0.5	-0.9	0.8	1.3
GNP Inflation Index	2.8	5.5	4.2	3.6	3.2	3.3	2.8	3.0	4.1	4.1	4.1	3.2	2.9
Consumer Prices	7.0	3.5	3.8	3.7	3.4	3.4	3.4	3.9	4.8	5.4	4.7	3.5	3.5
Value of the U.S. Dollar	-19.0	8.0	41.4	6.2	1.9	0.3	1.1	0.9	6.2	-9.6	2.3	3.7	-0.6
Percent													
Mfg. Capacity Utilization	80.8	78.1	77.4	77.7	78.2	79.0	79.9	80.6	83.9	82.3	77.8	80.2	83.2
Civilian Unemployment	5.9	6.5	6.8	7.0	7.1	6.9	6.7	6.6	5.3	5.5	6.9	6.7	6.2
Percent of GNP													
Federal Tax Receipts	20.4	20.5	20.5	20.5	20.5	20.7	20.7	20.7	20.2	20.3	20.5	20.7	20.7
Federal Expenditures	23.7	22.4	22.2	24.2	24.0	24.2	23.9	23.8	22.8	23.3	23.2	23.9	23.3
Federal Budget Deficit	-3.3	-1.9	-1.7	-3.7	-3.5	-3.5	-3.2	-3.1	-2.6	-3.0	-2.7	-3.2	-2.6
Interest Rates, Percent													
Federal Funds Rate	7.7	6.4	5.8	5.8	6.0	6.5	6.5	6.4	9.2	8.1	6.0	6.4	6.4
3-Month T-Bill Rate	7.0	6.0	5.6	5.6	5.7	6.2	6.2	6.1	8.1	7.5	5.7	6.1	7.8
Prime Rate	10.0	9.2	8.7	8.5	8.5	8.8	8.8	8.8	10.9	10.0	8.7	8.7	8.5
Discount Rate	6.9	6.2	5.7	5.5	5.5	5.8	6.0	6.0	6.9	7.0	5.7	5.9	6.0
Corporate AAA Bond Yield	9.3	8.9	8.7	8.5	8.4	8.5	8.6	8.5	9.3	9.3	8.6	8.5	8.1
30-Year Government Bond Yield	8.5	8.2	8.1	7.9	7.9	8.0	8.1	8.0	8.4	8.6	8.0	8.0	7.8
Mortgage Rates, Percent													
30-Year Fixed Rate	10.0	9.5	9.3	9.1	9.0	9.0	8.9	9.0	10.3	10.1	9.2	9.0	9.2
1-Year Adjustable	8.4	8.1	7.8	7.5	7.3	7.3	7.4	7.4	9.3	8.4	7.7	7.4	7.5
Home Sales & Starts													
Thousands													
Total Single-Family Sales (Single-family resales plus 97% of single-family starts)	3,879	3,778	3,875	4,119	4,264	4,427	4,474	4,526	4,442	4,179	4,009	4,497	4,649
Existing Single-Family Sales	3,117	3,080	3,146	3,303	3,411	3,520	3,545	3,583	3,467	3,305	3,235	3,564	3,660
New Single-Family Sales	470	461	516	534	573	582	600	611	654	533	521	604	645
Housing Starts	1,042	914	963	1,040	1,094	1,156	1,212	1,247	1,381	1,203	1,003	1,221	1,321
Single-Family Units	786	719	751	842	879	935	957	972	1,005	901	798	962	1,020
Multi-Family Units	256	194	212	198	215	221	255	275	376	302	205	259	301
2-4 Family Units	31	33	36	34	36	38	43	47	56	37	35	44	51
5+ Family Units	225	161	176	164	178	183	212	229	320	264	170	215	250
Mobile Homes Shipped	178	160	162	167	170	175	175	175	199	188	165	174	169
Percent change -- Year Ago													
Total Single-Family Sales	-13.8	-15.6	-8.5	-0.2	9.9	17.2	15.5	9.9	-4.4	-5.9	-4.1	12.2	3.4
Existing Single-Family Sales	-11.9	-10.6	-6.5	0.2	9.4	14.3	12.7	8.5	-3.6	-4.7	-2.1	10.2	2.7
New Single-Family Sales	-27.9	-22.8	-4.3	2.0	21.9	26.3	16.3	14.4	-3.3	-18.5	-2.2	15.9	6.8
Housing Starts	-22.9	-36.3	-20.0	-8.0	4.9	26.5	25.9	20.0	-7.2	-12.9	-16.6	21.8	8.2
Single-Family Units	-20.9	-32.4	-16.2	-1.7	11.8	30.0	27.4	15.5	-7.2	-10.4	-11.4	20.6	6.0
Multi-Family Units	-28.4	-47.3	-31.3	-27.8	-16.2	13.7	20.5	38.9	-7.2	-19.7	-32.2	26.4	16.3
2-4 Family Units	-42.2	-23.3	-17.1	5.1	17.6	13.7	20.5	38.9	-5.1	-32.8	-6.9	26.4	16.3
5+ Family Units	-26.0	-50.5	-33.6	-32.1	-20.8	13.7	20.5	38.9	-7.6	-17.4	-35.8	26.4	16.3
Median Home Prices													
Thousands of Dollars													
Existing Home Prices	92.2	95.4	96.7	97.7	98.3	100.0	101.4	102.8	92.9	95.2	97.0	102.0	107.2
New Home Prices	122.0	124.5	125.8	126.9	128.8	131.1	132.5	134.1	120.4	122.3	126.5	133.4	140.2
Percent Change - Year Ago													
Existing Home Prices	-0.5	-0.1	0.1	1.1	6.6	4.9	4.8	5.3	4.2	2.4	1.9	5.2	5.1
New Home Prices	-2.0	0.6	-0.7	8.7	5.6	5.3	5.4	5.7	6.2	1.6	3.4	5.4	5.1

Forecast produced using Laurence H. Meyer & Associates' model of the U.S. economy. Assumptions and simulations by Dr. John Tuccillo, Robert Barr and Kimberly Martin.

The *Real Estate Outlook* features a monthly summary of current economic conditions, an easy-to-read forecast for the economy and real estate, and selected reports on issues affecting the housing industry. In addition, one of the Nation's top real estate economists, Dr. John Tuccillo, gives his commentary on the state of the economy and its implications for real estate markets. If you would like to subscribe to the *Real Estate Outlook*, contact the Forecasting and Policy Analysis Division at (202) 383-1131. The annual subscription fee is $25 for members of the NATIONAL ASSOCIATION OF REALTORS® and $30 for nonmembers.

A-7000-1

Real Estate OUTLOOK

June 1991

May's payroll employment gain is the most recent of many signals pointing to an imminent recovery. The month's addition of 49,000 workers to private payrolls was the first increase in the past eleven months. Even if it is at hand, however, the recovery is expected to be far from robust. Lackluster consumer spending and personal income gains may prevent any rebound from gaining a firm toehold. Growth in the second half of 1991 is estimated at 2.3%. *Page 2*

For the third consecutive month, the annual rate of existing home sales increased, rising 3.4% in April to an annual sales rate of 3,330,000 units. This pace is the fastest clip in the sales rate since last August. A sign that the Northeast is overcoming its housing slump is the region's gain of 12.8% in its sales rate from March. It now stands almost 4% higher than the level recorded a year earlier. *Page 6*

The median price of existing homes rose over the $100,000 level for the first time. April's 2.0% increase put the price at $100,200 and 4.7% above its level of one year ago. It was only the fourth increase in the past twelve months, but the third gain in the last four. *Page 7*

Also In This Issue:

Demography, Destiny & Economics — *Economic Commentary by John A. Tuccillo*

Outlook for the Economy & Real Estate — *Robert D. Barr & Kimberly A. Martin*

Charting The RTC's Progess: Impacts on Real Estate Markets — *Kimberly A. Martin*

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Demography, Destiny and Economics

by John A. Tuccillo
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On May 23, Bob Dylan turned fifty. But in reality, he's more like 25, frozen in amber for those who came to him and his music at a time when they were puzzling about life and change and independence. Dylan's early work was much more diverse (although less polished or melodious) than the stuff he's done for the last decade or so. It ranged from the familiar protest stuff ("Blowin' in the Wind") to the traditional folk ballad ("North Country Blues") to love songs ("To Ramona") to pure whimsy ("All I Really Want to Do"). But the common thread was the ability of his rasping, nasal voice to capture the imagination of a generation that wanted nothing more than to change the world.

Well, it did, but not in the way it thought. In fact, even before Dylan began to play the coffee houses of Greenwich Village (where millions now claim to have heard him) or burst on the music scene at the Newport Folk Festival, they had already changed the world. For, simply because of its size, the postwar generation has been the driving force in virtually every economic and social event in this country for the past forty plus years. They have been a moving revolution that has shaped the economy we live in, and they will continue to do so in the Nineties.

The Fifties were a decade of growth and migration. We lived less and less in cities and on farms and more and more in the strange new world of suburbia. Part of this derived from the unchallenged economic preeminence of the United States. But even more so, change was predicated on the desires for new family-builders to provide "the best" for the kids. So we built houses and roads and schools and hospitals and all those things that fit the lives of families with young children. Individual firms and whole industries also bloomed. Television came into the house through the kids.

The Sixties are a decade we most often associate with the power of the postwar generation, and it was here that the need for these folks to change the world was born. But the function of adolescents in society has always been to challenge authority. The fact that this generation was so large legitimized that function and caused it to dominate a decade.

That decade featured an economy that became youth-oriented; those industries that catered to the young grew the fastest. Even more importantly, the optimism of the time and the social and political ferment generated by the young opened a new era of government activism that very clearly established the Federal budget as an instrument of economic and social policy.

But the world did not change in the Sixties. When the Seventies dawned, this postwar generation had to go to work, and like a great wave, they crashed on the shore of the labor market and swamped it. The Seventies saw inflation and sluggish economic growth, again the product of a large number of untrained workers.

The surfeit of labor had another impact, as well. At a time when our newly found competitors in Europe and Asia were recapitalizing and adopting cutting edge productive technology, and at a time when our own capital stock was beginning to show signs of wear, industry was reluctant to rebuild itself; it was far more easy to substitute labor for capital. Ultimately, this has cost the American economy by reducing its long run growth and increasing the cost of replacing completely exhausted machinery.

In the Eighties, these folks got the hang of their jobs, settled down and became productive (in both the economic and the genetic sense). They earned more and spent more, and the economy grew. But because we had not made the necessary capital improvements in the prior decade, that spending increasingly was devoted to goods produced abroad. Japanese and German producers used a more advanced capital stock to turn out quality that was very appealing to these semi-affluent young adults.

Another interesting thing was happening as well. These folks were pushing back the traditional American calendar. They got married later in life (if at all) and had families later. They bought homes later. So the typical demographic progression was replaced by a consumption ethic that looked a great deal like the Twenties.

So where are we in the Nineties (stuck inside of Mobile with those Memphis blues again?) This decade will be little different from the past four. That huge population surge that occurred forty years ago will still shape the economy. Only now it is reaching what we once called middle age (let's say "chronologically gifted") and the generation that once dropped acid to escape reality is now dropping antacid to cope with it.

This suggests a somewhat better and more even economy than we are used to. As it ages, the postwar generation will pass through the peak of its productive powers and into its high saving years. This ought to bias the economy toward lower interest rates and consistent growth, allowing us to renew our capital stock and regain a strong competitive position in an interdependent world economy.

The real estate market will feel this transition as well. As they age, these households will adjust their housing consumption. The four bedroom, center hall colonial American Dream will be replaced in their affections by the high amenity, low maintenance, smaller unit that lies within easy reach of the golf course or the beach or the mountains or the museum.

As George Will put it, "In a democracy, demography is destiny." So it has been for the past four decades in the American economy, and so it shall be in the Nineties. And it looks like a decade of settling in. Ultimately, 1991 may be remembered by the postwar generation more as Cole Porter's centennial than Bob Dylan's fiftieth. And that would be because they've finally thrown off the gloomy concerns of the Sixties for a brighter view of their world. Ah, but they were so much older then; they're younger than that now.

Outlook for the Economy

Beneath the smoke and haze of recent economic statistics, the first tentative flames of recovery appear to be flickering. Existing home sales have increased for the fourth consecutive month, payroll employment increased in May, and construction spending was up, to name a few of the measures pointing toward recovery. Keeping a careful eye on the campfire is the Federal Reserve, who's concerned with stoking it too much but also mindful of the wet logs of tax increases, high consumer debt burdens, the commercial real estate slump, and the defense industry retrenchment. To feed the fire, the recovery needs healthy gains in personal income and employment. Will the flames spread, or will they burn themselves out?

Chances are that the recovery will spread. The statistics signal a recovery that is imminent, if it hasn't already arrived. After falling at an annual 2.6% rate in the year's first quarter, production in the U.S. economy, or real GNP, is expected to post a slight 0.2% increase in the second quarter. The rebound will gather steam during the second half of 1991, when growth is expected at a 2.3% clip. For the year, real GNP will fall 0.3%, down from 1990's modest 1.0% rate. Recovery will continue in 1992, with output growth of 3.0% expected.

Good News From The Labor Market

The strongest sign of recovery came from the release in early June of May's employment picture. Private payroll employment climbed by 49,000 workers, the first increase since last June (see chart). The gain was a relatively small one compared to the average increase tallied during the expansion of the 1980s, but it comes after an average decline of 242,000 workers over the previous four months. The unemployment rate, which is calculated from a survey that is separate from the payroll data, rose to 6.9% from 6.6% in April. Given the gain in payrolls, this increase is not alarming; since the labor force usually grows faster than the number of jobs early in recoveries, such jumps in the unemployment rate are common.

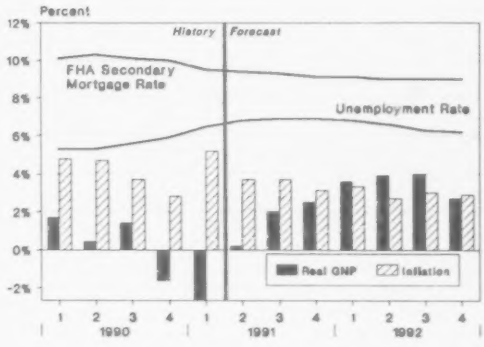
Other measures showing an advancing economy include the housing markets, discussed in depth on pages 4-7. The monthly index on industrial activity prepared by the National Association of Purchasing Management has increased for the fourth consecutive month, and the government's index of leading indicators has a three-month string of increases -- usually a sign of a waning recession.

On The Lookout for the Double Dip

Even if it is at hand, the recovery is far from robust at this stage. The recent spurt of activity may dissipate, with the economy heading back down in a "double dip." The failure of the economy to generate enough momentum to sustain a rebound is not uncommon, and even a positive rate of economic growth in the second quarter does not mean that we've put the recession behind us.

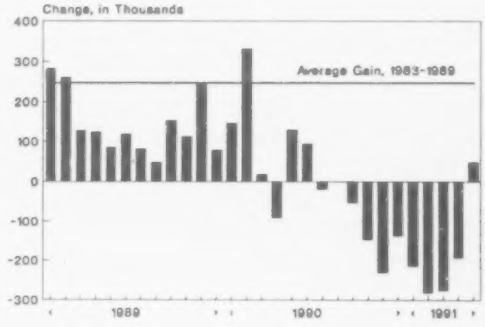
The incipient recovery could be choked off by higher interest rates, lower overseas demand, or some external shock such as higher oil prices or drought. Or the lack of consumer enthusiasm may snuff it out. The consumer spending chart shows gains in February and March, as prewar jitters were calmed by the overwhelming success in the

The Economic Outlook

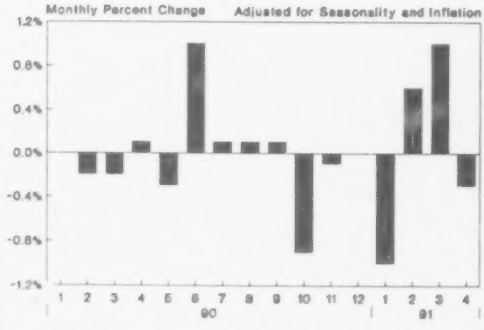


Employment Reverses Course. . .

First Gain in the Past 11 Months



. . .But Consumption May Not Be Back On Track



Gulf War. But April sported a decline, suggesting that the burst of spending from pent-up demand was over. May's results on spending are not yet available, but consumer confidence surveys taken during the month point to another dismal performance.

Another important factor that will keep the recovery subdued is an industry which will not be rescued by the tonic of lower interest rates. The defense industry is shrinking, and this movement from guns to butter is an important structural shift in the economy. While less spending on defense means that more resources can be channeled elsewhere in the economy -- a smaller federal deficit or more federal domestic spending, for example -- the transition will be painful for some companies and regions.

Fed Not Expected to Ease Further

With signs that the recovery is around the corner, the Fed is much less likely to ease monetary credit further. Short-term rates, which are heavily influenced by Fed credit moves, have already fallen over two percentage points since the beginning of the recession, as shown on the chart at right.

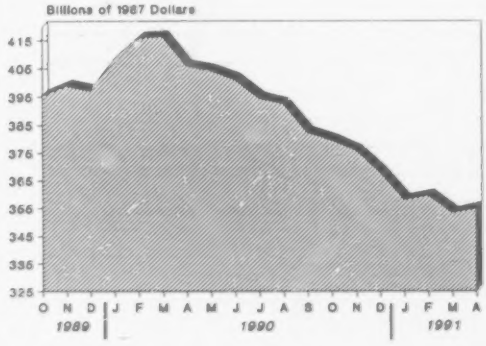
The Fed thinks it's done about as much as it can do. Since a change in credit policy takes several months to work its way through the economy, easing today could spur the economy late this year -- after we are well into a recovery. In other words, it's too late for extra credit stimulation now to end the recession. While it might provide insurance against another slump, the premium is high: additional inflationary pressure later. And fighting inflation remains the Fed's chief concern.

The graph also shows that long-term rates have been stubborn in falling. In fact, they've moved up in recent days. Lower long-term rates would insure a stronger recovery, but the Fed does not have the leverage to pull those down. Since these rates depend in large part on market expectations about inflation, and since we expect inflation to ease over the forecast horizon, there's room for these long-term rates to fall. Continued good news on inflation and a steady Fed hand on the monetary rudder will reverse the recent uptick in rates and go a long way to bringing us lower rates by year-end. Yields on the 30-year Treasury bond, which averaged 8.4% in the week ending June 7, are expected to fall to 8.0% during the third quarter.

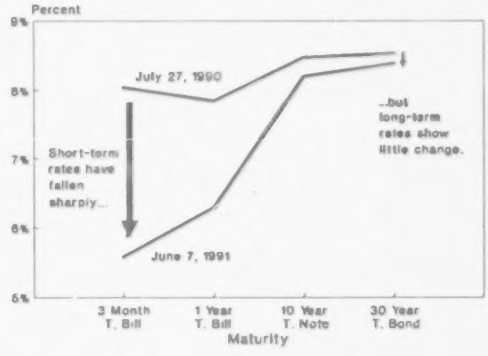
Recovery May Still Feel Like Recession

In many ways, determining the exact onset of the recession may be only an academic exercise since growth is expected to remain sluggish at least through 1991. Despite the relatively mild recession, the U.S. economy is slogging through an uncommonly long period of subpar economic growth, as seen at the chart at right. Since early 1988, the economy has not had even one quarter of growth that exceeded the average growth rate achieved during the 1983-89 period. A subdued recovery will continue this pattern through 1991, with growth only nearing average in 1992. Five years of mediocre performance is a weak foundation for growth in jobs, personal income, and housing, among other areas of the economy. In many ways, it may feel as though the recession is lingering.

Construction Spending May Have Hit Bottom

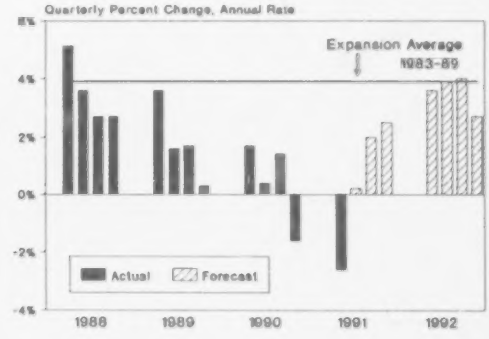


Movement in Short- and Long-Term Interest Rates



GNP's Sub-Par Performance

Below-Average Growth: Four Years and Counting



Housing Starts

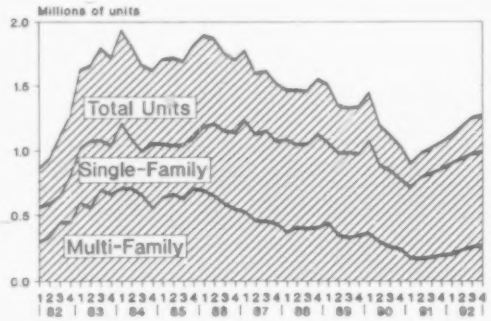
National Data

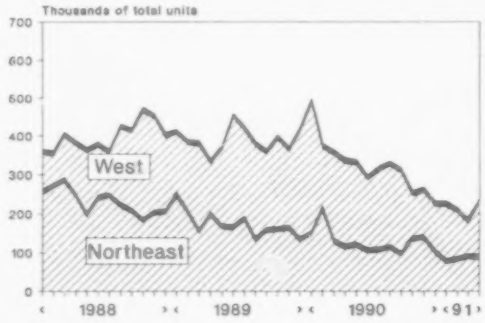
	Total	SF	MF:2-4	MF:5+
Apr 1990	1,217	901	51	265
Nov 1990	1,130	769	54	307
Dec 1990	971	751	17	203
Jan 1991	847	648	29	170
Feb 1991	992	788	37	167
Mar 1991	901	736	26	139
Apr 1991	***957***	***778***	***41***	***138***
Annual Averages:				
1989	1,381	1,005	56	320
1990	1,203	901	37	265
Percent Changes in April 1991 since:				
Apr 1990	-21.4	-13.7	-19.6	-47.9
Mar 1991	6.2	5.7	57.7	-0.7

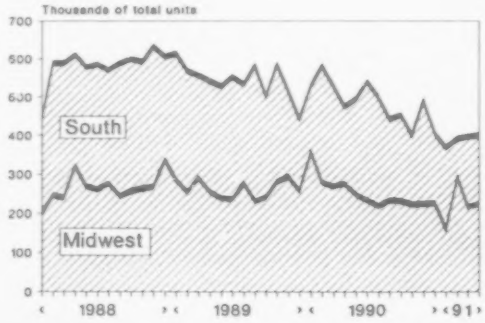
Regional Data

	Northeast	Midwest	South	West
Apr 1990	124	283	467	343
Nov 1990	147	232	483	268
Dec 1990	110	233	395	233
Jan 1991	86	167	361	233
Feb 1991	91	301	384	216
Mar 1991	98	224	389	190
Apr 1991	***96***	***231***	***392***	***238***
Annual Averages:				
1989	181	269	535	397
1990	135	259	478	330
Percent Changes in April 1991 since:				
Apr 1990	-22.6	-18.4	-16.1	-30.6
Mar 1991	-2.0	3.1	0.8	25.3

Levels are seasonally adjusted annual rates, in thousands.
Source: Bureau of the Census, Construction Reports, Series C25







After retreating in March, housing starts increased in April by 6.2% to an annual rate of 957,000 units. This figure remains more than one-fifth below the April 1990 starts pace of 1,217,000 units. The increase was spread almost evenly between the construction of single and multifamily homes. Single-family housing starts increased to an annual rate of 778,000 units, which is 5.7% above the March figure of 736,000 units. The construction of multifamily homes was up from March by 8.5%, to an annual rate of 179,000 units.

The national gain was not well distributed among the four Census reporting regions. Accounting for over 85% of the total increase was the West region, where starts grew by 25.3% to 238,000 units. Despite the boost, the starts pace in the region remains off by almost one-third from its pace of a year ago. Construction also rose in the Midwest, where starts increased 3.1% from March to 231,000 units. Starts in the South edged up 0.8% to 392,000 units. In the Northeast, construction activity waned as starts slipped by 2.0% to an annual rate of 96,000 units.

With the approaching recovery, total housing starts in the second quarter will post a healthy 8.3% gain over the first quarter's rate. Lower mortgage rates and the belief that the end of the recession is at hand will boost construction by 76,000 units. By the third quarter of 1991, starts are expected to surpass the one million mark. In 1992, economic expansion and the easing of the credit crunch are expected to pull multifamily starts up by 30.6% and single-family starts up at a 19.1% clip. Overall, starts are expected to be 21.3% higher in 1992 than in 1991.

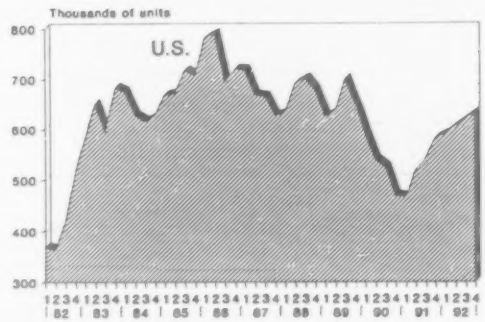
National Data

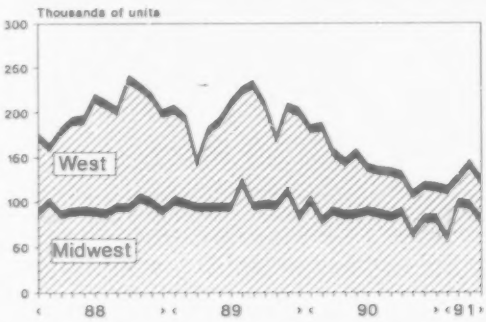
		Mo. Ago % Chg.	Yr. Ago % Chg.
Apr 1990	534	-4.5	-12.5
May 1990	535	0.2	-17.8
Jun 1990	549	2.6	-15.0
Jul 1990	541	-1.5	-27.0
Aug 1990	525	-3.0	-27.0
Sep 1990	504	-4.0	-21.0
Oct 1990	465	-7.7	-26.9
Nov 1990	480	3.2	-30.1
Dec 1990	464	-3.3	-26.7
Jan 1991	414	-10.8	-34.0
Feb 1991	489	18.1	-19.3
Mar 1991	494	1.0	-11.6
Apr 1991	***500***	*1.2*	*-6.4*
Annual Averages:			
1989	654		-3.3
1990	534		-18.3

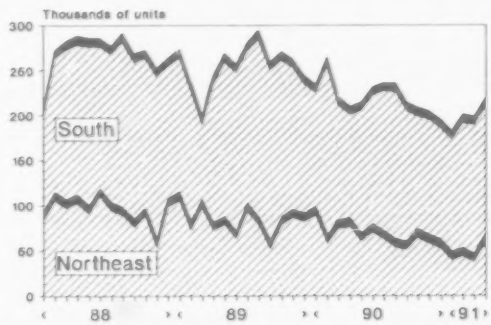
Regional Data

	Northeast	Midwest	South	West
Apr 1990	86	90	210	149
Nov 1990	68	86	205	122
Dec 1990	62	86	195	121
Jan 1991	49	65	183	118
Feb 1991	53	103	201	131
Mar 1991	47	101	199	147
Apr 1991	***69***	***84***	***219***	***128***
Annual Averages:				
1989	90	103	258	202
1990	75	90	222	147
Percent Changes in April 1991 since:				
Apr 1990	-19.8	-6.7	4.3	-14.1
Mar 1991	46.8	-16.8	10.1	-12.9

Levels are seasonally adjusted annual rates, in thousands.
Source: Bureau of the Census, Construction Reports, Series C25







The Northeast region led the nation in the increase in the sales rate of new homes in April. The Northeast saw a dramatic 46.8% increase from March's dismal level of 47,000 units. Following the Northeast's lead, the South also recorded a healthy sales pace. There, sales increased 10.1%, driving the annual rate of sales up to 219,000 units. These sharp increases are in contrast to declines in the Midwest and the West. Sales in the Midwest fell 16.8%, dropping below the 100,000 mark to 84,000 units. The West's 12.9% decline put the annual rate at 128,000 units. The disparate regional performances collectively translate into a national increase of a modest 1.2%. After six consecutive months under the half-million mark, sales in April just reached that plateau. The April sales figure is 6.4% below the figure recorded in April of 1990.

The April figures support the view that January's poor performance will be the nation's low point. The ensuing recovery is reflected in the NAR forecast for new home sales. As early as the second quarter of 1991, new home sales are expected to be on the rise, gaining 53,000 units over the first quarter. By the fourth quarter of 1991, new home sales are expected to be 24.7% higher than the first quarter's rate. Overall, new home sales are expected to average 527,000 units in 1991, which is scarcely below 1990's rate of 533,000 units.

In 1992, sales are expected to grow at a healthy clip, leaving the year with a sales rate more than 16% greater than 1991's projected rate. Despite the growth, this sales rate of 612,000 new homes will be about 6% below 1989's level.

Existing Home Sales

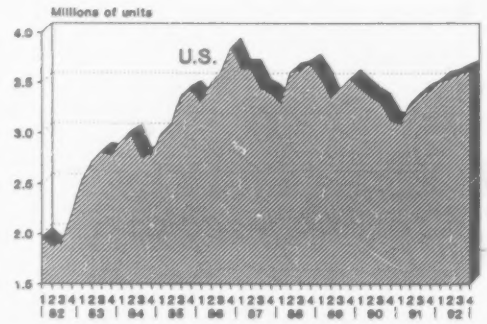
National Data

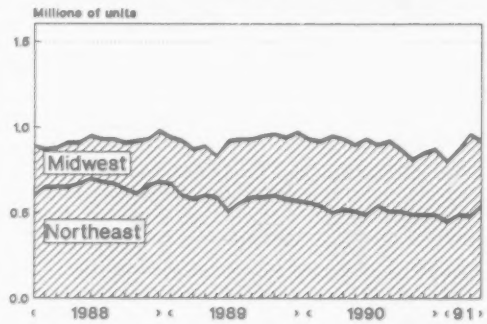
		Mo. Ago % Chg.	Yr. Ago % Chg.
Apr 1990	3,370	-2.0	-2.0
May 1990	3,350	-0.6	-2.0
Jun 1990	3,370	0.6	3.1
Jul 1990	3,320	-1.5	1.2
Aug 1990	3,410	2.7	-1.8
Sep 1990	3,160	-7.3	-0.9
Oct 1990	3,070	-2.8	-10.0
Nov 1990	3,150	2.6	-12.0
Dec 1990	3,130	-0.6	-11.5
Jan 1991	2,900	-7.3	-12.1
Feb 1991	3,160	9.0	-16.4
Mar 1991	3,220	1.9	-7.6
Apr 1991	***3,330***	***3.4***	***-6.4***
Annual Averages:			
1989	3,440		-4.3
1990	3,293		-4.3

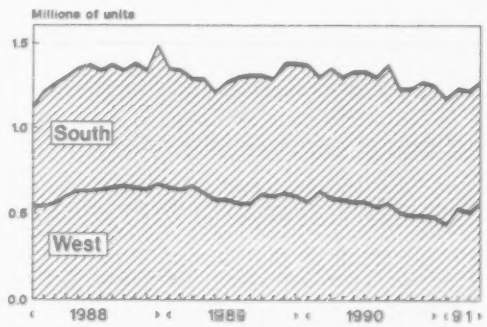
Regional Data

	Northeast	Midwest	South	West
Apr 1990	530	940	1,310	590
Nov 1990	500	860	1,280	500
Dec 1990	500	880	1,260	490
Jan 1991	460	810	1,180	450
Feb 1991	500	880	1,240	540
Mar 1991	490	970	1,230	520
Apr 1991	***550***	***930***	***1,280***	***570***
Annual Averages:				
1989	589	919	1,307	610
1990	517	896	1,310	569
Percent changes in April 1991 since:				
Apr 1990	3.8	-1.1	-2.3	-3.4
Mar 1991	12.2	-4.1	4.1	9.6

Levels are seasonally adjusted annual rates, in thousands.
Source: National Association of Realtors®, 'Home Sales'







The rate of existing home sales increased for the third consecutive month and reached its highest level since last August. Following increases of 9.0% in February and 1.9% in March, sales of existing homes climbed another 3.4% in April. Consequently, sales have recovered almost 15% from its low point in January 1991. The annual resale rate for April stands at 3.33 million units and is 6.4% below the figure recorded in April of 1990.

Only the Midwest failed to post a gain in resales during April. In the Northeast, sales of existing homes displayed the greatest strength, increasing a healthy 12.2% from March's 490,000-unit rate. One tentative sign of economic recovery in the Northeast is that the rate of 550,000 units was more than 5% greater than the average sales rate in the region during 1990. The rate increased 9.6% in the West, totalling 570,000 units, while in the South, sales gained 4.1% to an annual rate of 1.28 million units. The rate of existing home sales dropped 4.1% to an annual rate of 930,000 units in the Midwest.

According to the NAR forecast, existing home sales are expected to increase 6.4% between the first and second quarters of 1991. Thereafter, sales are expected to continue to grow at a healthy clip, reaching an annual rate of 3.43 million units by the fourth quarter of 1991. As economic recovery takes hold, existing home sales will be positioned for robust growth. In 1992, sales are projected to increase 8.1% to 3.57 million units. Sales will continue to increase in 1993, but will experience a slight deceleration, increasing a modest 3.1% to 3.68 million units.

National Data

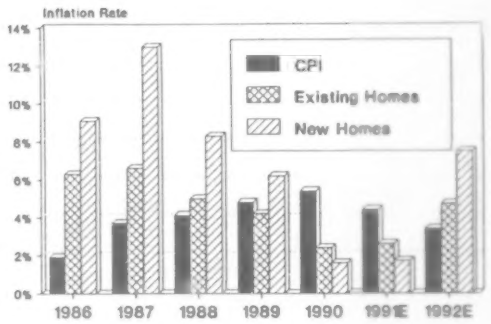
	Median		Average	
	Existing	New	Existing	New
Apr 1990	95,700	130,000	117,900	153,400
Nov 1990	92,000	118,900	115,600	144,800
Dec 1990	91,700	127,000	114,100	153,400
Jan 1991	95,600	117,900	123,000	148,600
Feb 1991	94,000	120,000	119,700	148,900
Mar 1991	98,200	123,300	125,200	157,700
Apr 1991	***100,200***	***122,000***	***128,400***	***155,400***
Annual Averages:				
1989	93,100	120,400	118,100	148,300
1990	95,500	122,300	118,600	149,100
Percent changes in April 1991 since:				
Apr 1990	4.7	-6.2	8.9	1.3
Mar 1991	2.0	-1.1	2.6	-1.5

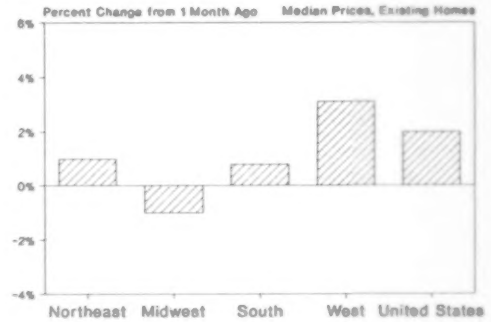
Regional Data

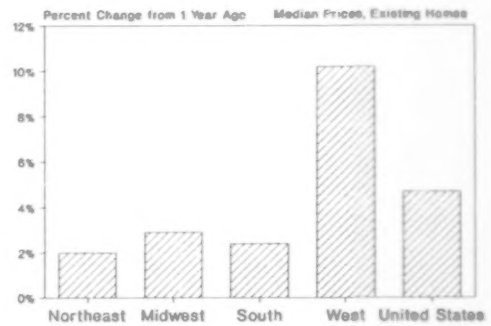
Median Prices for Existing Single-Family Homes

	Northeast	Midwest	South	West
Apr 1990	141,300	75,200	85,900	137,800
Nov 1990	134,200	71,800	83,500	139,600
Dec 1990	134,400	72,300	82,800	131,400
Jan 1991	136,900	74,500	84,600	149,600
Feb 1991	137,200	76,400	83,200	137,100
Mar 1991	142,700	78,200	87,300	147,300
Apr 1991	***144,100***	***77,400***	***88,000***	***151,800***
Annual Averages:				
1989	145,200	71,300	84,500	139,900
1990	141,200	74,000	85,900	139,600
Percent changes in April 1991 since:				
Apr 1990	2.0	2.9	2.4	10.2
Mar 1991	1.0	-1.0	0.8	3.1

Levels are shown in dollars.
Source: National Association of Realtors®, 'Home Sales'







The national median price of existing single-family homes topped the $100,000 level for the first time in April. The month's $2,000 increase put the price at $100,200, 4.7% above the median price of a year ago. It was only the fourth increase recorded in the past twelve months, but the third gain in the last four.

In the market for new homes, the median price declined 1.1% to $122,000 in April. The median price of a new home is 6.2% below the figure of a year ago, but the recent trend in the price is not very clear. It has fallen in seven of the past twelve months, ranging from a low of $113,000 to a high of $127,000.

The average price of an existing home increased by 2.6% in April to $128,400. Since April of 1990, the average price has risen 8.9%. A decline of 1.5% in April resulted in a loss of $2,300 to the average price of a new single-family home.

Modest appreciation in the median price of an existing single-family home is expected over the next year, with an overall increase of 2.6% in 1991. Prices are expected to firm in 1992 and should increase 4.7% in 1992. The price appreciation of a new single-family home is projected to modestly accelerate in 1991, with prices increasing only 1.7% in 1991. In 1992, however, the median price of a new single-family home is expected to appreciate with renewed force, increasing 7.5% to $133,600.

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Charting the RTC's Progress:

Impacts On Real Estate Markets

Introduction: The insolvency of many of the nation's savings and loan associations presented Congress with a Gordian knot. The industry became entangled as a result of the changing economic environment throughout the last few decades. The high inflation of the Seventies, high interest rates, changes in government regulation, and oil booms and busts in the southwestern United States culminated in the current crisis. The most daunting task in restoring financial stability to the industry is liquidating failed thrifts' assets, particularly the vast amount of real estate properties.

To resolve insolvent thrifts, Congress created the Resolution Trust Corporation (RTC) in August, 1989. The purpose of this progress report is to review the performance of the RTC, while paying particular attention to issues surrounding real estate markets. A summary of the events leading up to the savings and loan crisis and the government's policy solution to the crisis will set the stage for review. Two measures of performance are considered in this progress report. A measure of the RTC's results to date, including a description of the asset portfolio and a detailed break out of sales, is presented first. Another measure, which is perhaps more telling, examines the obstacles encountered by the RTC in selling real estate and their strategies to overcome them. Also considered is the economic impact of a large number of property sales over a short span of time within a local market, known as *dumping*. Our analysis will then take a slightly different turn and consider the RTC's provisions for affordable housing. We will conclude with a brief discussion of working with the RTC.

Historical Perspective: The savings and loan industry was created during the 1930s to service the home mortgage market. Up until 1980, savings and loan associations dealt almost exclusively in residential mortgage lending. For the most part, this provided a safe and comfortable existence. There were, however, two weak links in the accounting structure. First, thrifts were making long-term, fixed-interest-rate mortgage loans, and funding these with short-term liabilities -- typically, passbook deposits that could be withdrawn on demand. Second, deposits were uniformly insured by the Federal Savings and Loan Insurance Corporation (FSLIC), which used regulatory oversight, not risk-based premiums, to discourage risky investments.

This arrangement lasted only as long as interest rates and inflation remained low and thrift failures were few. By the late-1970s, the first weak link frayed when interest rates jumped due to increasing inflation. Since thrifts were limited in their ability to raise interest rates to attract deposits, funds flowed to other interest-bearing assets, such as money market mutual funds. As a result, losses in the thrift industry became excessive.

To shore up these losses, the government loosened regulations and created incentives for thrifts to diversify away from residential mortgage lending. However, many of these investment opportunities were risky and, combined with loosened government regulation, exacerbated the problems created by rising interest rates. By the late 1980s, weaker economic performance and falling real estate values exposed the poor quality of many of these loans. As a result, many thrifts became insolvent, forcing the FSLIC to honor the thrifts' obligations to depositors. Inadequate FSLIC reserves required the U.S. taxpayer to make up the difference.

Government Response: Longstanding problems in the savings and loan industry combined with the insolvency of the FSLIC demanded that the federal government take direct action. Congress responded with the Financial Institutions Reform,

Recovery and Enforcement Act (FIRREA) on August 9, 1989. FIRREA provided for a major reorganization of the federal regulatory agencies which oversee the savings and loan industry. Both the FSLIC and the Federal Home Loan Bank Board (FHLBB) were replaced with the newly created Office of Thrift Supervision (OTS) and the RTC. The OTS has supervisory and regulatory authority over savings and loan associations, and governs the operation of the RTC.

The RTC has control over all FSLIC-insured thrifts which have become, or will become, insolvent between January 1, 1989 and August 9, 1992. When an institution is determined to be insolvent, it is designated as either a conservatorship or receivership institution.

A conservatorship institution is managed by an RTC-appointed conservator. A conservator works, on a day-to-day basis, with the owners and managers of the insolvent thrift to restore its financial stability. In so doing, the RTC will often require a conservatorship institution to liquidate some of its assets. In the case of a conservatorship, thrift owners and managers maintain an active role in the day-to-day operation of the insolvent thrift, including the liquidation of some of the thrift's assets.

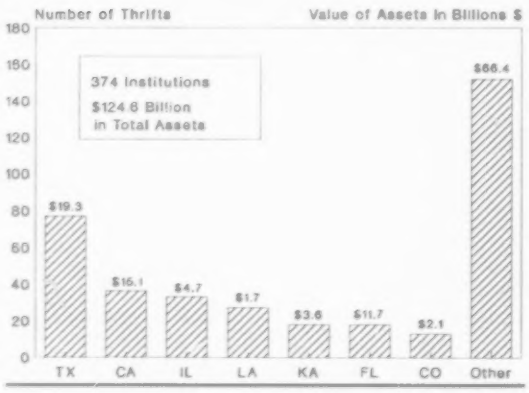
When the RTC determines that financial stability cannot be restored to an insolvent thrift, whether it has been under conservatorship or is a newly acquired thrift, it is placed under the RTC's receivership program. Unlike a conservatorship, a receivership is placed under the complete control of the RTC. A receivership institution is closed to the general public, and is no longer able to accept new deposits or make new loans. The RTC's goal is to liquidate all assets, going so far as to auction the computers and furnishings of the receivership institution. Thrift owners and managers neither play a role in the day-to-day operation of the thrift, nor do they assist in the sale of assets. The assets of a receivership are sold directly by the RTC.

Results to Date: As of March 31, 1991, the RTC has disposed of $148 billion in assets from 578 insolvent thrifts. The RTC has sold $70.1 billion in securities, $55.1 billion in mortgages, $12.1 billion in nonmortgage loans, $4.4 billion in real estate, and $5.8 billion in other assets.

Of the thrifts under RTC control, 204 are

Geographic Distribution of Receiverships

Value of Assets at Time of Closure



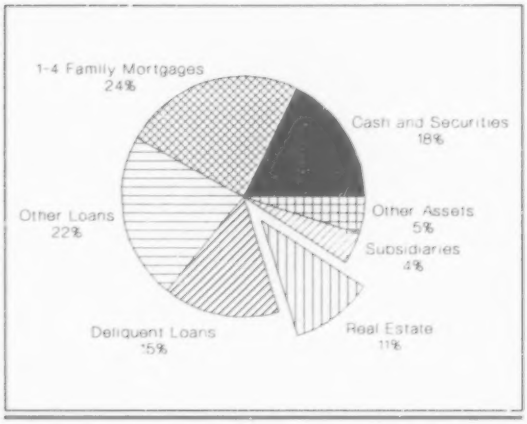
conservatorship institutions. The remaining 374 are receivership institutions which have been closed by the RTC. More than half of the closed thrifts were located in Texas, California, Illinois, Louisiana, Florida, and Kansas. In resolving the 374 receivership institutions, 194 were purchase and assumption transactions (P&As). Using this approach, the RTC sold all deposits, selected liabilities, and a portion of the assets to acquirers. An additional 128 cases were insured deposit transfers (IDTs), whereby acquiring institutions established accounts for the depositors of failed institutions and acquired some of the failed thrifts' assets. The remaining 52 cases were insured deposit payouts (POs) in which the RTC directly paid depositors their insured deposits and retained all of the assets from the failed thrifts.

The RTC holds an additional $161.9 billion in assets that it hopes to sell off. Of this total, the RTC has retained $69.3 billion in assets from the 374 receivership institutions, and $92.6 billion in assets from the 204 institutions under conservatorship. The assets under RTC control include 45,172 commercial, residential and recreational properties.

Portfolio Description: A significant portion of the thrift assets under RTC control are relatively liquid, performing assets such as single-family mortgage portfolios and other loans and government securities. Typically, these assets are transferred or sold to other financial institutions together with the transfer or sale of the

The RTC's Portfolio of Assets

Percentage of Total Dollar Value



institutions' franchises and their deposits. The RTC also must dispose of a continually growing number of non-performing assets. Most non-performing assets are real estate properties, such as residential homes, hotels, office buildings, shopping centers, and undeveloped land. Because they were either abandoned before completion or have remained vacant since foreclosure and have deteriorated, many of the non-performing real estate properties are of inferior quality. The purchase of these properties requires a buyer to have the resources to make a downpayment on the property and to invest 10% to 20% of the property value to bring it up to acceptable condition.

Seller Financing: The sale of commercial real estate and bulk residential property has also been hampered by a lack of sufficiently available third-party financing. The RTC believes that the sale of much of its land and commercial real estate property can be facilitated by providing financing itself.

In financing a sale, the RTC provides the purchaser with a loan in the amount necessary to consummate the sale of the property. In the fashion of the well established secondary market for residential mortgages, the RTC plans to work with the secondary market to securitize commercial loans for resale to private investors. This requires that the terms of the loan be written to suit the secondary market.

Up until recently, the RTC had a small scale seller-financing plan which did not adequately meet the demand for seller-financed sales. Seller financing was previously available only for real estate and mortgage sales, with a total $1.25 billion limit. In early December, 1990, the RTC Oversight Board approved a revised seller-financing plan. Seller financing was expanded to include real estate assets, non-performing loans, and high yield securities, with a total $7.0 billion limit. This limitation applies to all loans originated by the RTC which are outstanding. Of this amount, a minimum of $250 million has been allocated for the RTC's Affordable Housing Disposition Program.

Seller financing is available for transactions whose sales price equals or is in excess of $500,000. This minimum transaction price reflects the value of the RTC's inventory of commercial real estate properties, many of which are valued above $500,000. The policy applies uniformly to all illiquid assets. Assets are deemed illiquid based on two criteria: First, due to a lack of available commercial funding on acceptable terms, the RTC determines that an asset isn't readily marketable. Second, the RTC determines that competitive marketing of the asset has already occurred and that a seller financed sale will bring a greater return than other alternatives such as a cash sale, securitization, or a deferral of the sale.

The RTC prefers a down payment of 25%, but will consider down payments as low as 15% of the sales price. On a case-by-case basis, the RTC will consider allocating a 15% commitment between a down payment and a funded escrow to be used for capital improvements on the property. Because of the poor quality of many of the RTC's properties, below-market financing may often be requested, but the RTC's policy is to set interest rates which equal prevailing mortgage rates. The sale of single and multifamily properties under the Affordable Housing Disposition Program has a separate set of guidelines, which will be outlined later.

Auctions: A second strategy adopted by the RTC in returning real estate assets in a timely manner to the private sector is auctioning. Since many properties are offered up for sale at one time, auctions can provide for the rapid disposition of the RTC's inventory of real estate assets. There is, however, a potential downside to the auctioning process. Unloading many properties at once onto a local market at below-market prices may lower